OWE'S BOOKKEEPING ND ACCOUNTANCY

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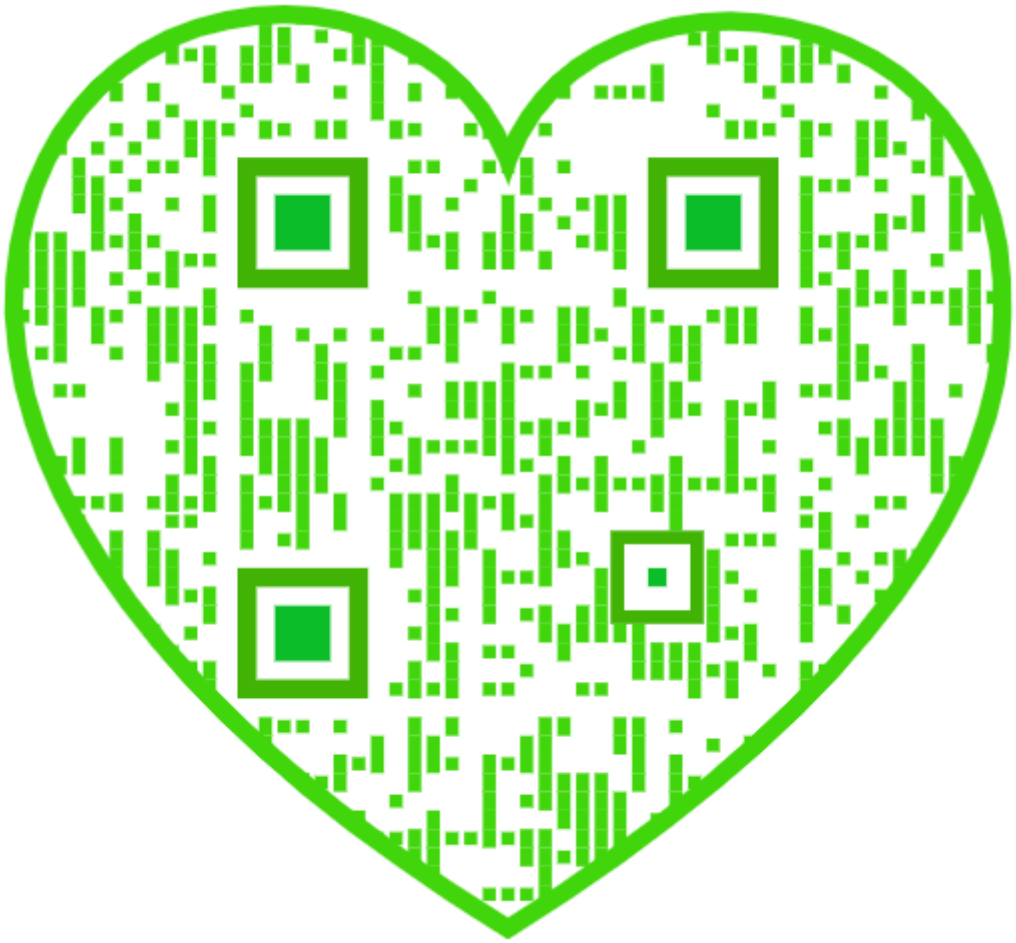

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Bookkeeping and Accountancy

Presenting the art of bookkeeping in accordance with the principles of modern accountancy

By

HARRY M. ROWE, Ph.D.

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SCRIPT BY C. P. ZANER

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PREFACE.

"Bookkeeping and Accountancy" is intended to impart a training in the art of bookkeeping that is based upon the fundamental principles of accountancy. It is intended for students of the age usually found in commercial schools, public and private, who are ready to begin a study of the subject. The completion of the full course of study provided will not only qualify for a high degree of proficiency in the art of bookkeeping, but it will also lead up to a very thorough understanding of the general principles and practices of accountancy.

While for many years I have closely followed the development of accountancy as a science, particularly in its economic relations, I am no longer a practicing accountant, therefore, I have presented accountancy in this work as I have found it, particularly as reflected in the practical experience of many eminent accountants with whom I have consulted.

My principal task has been to simplify the presentation of accountancy so that it may be understood by the average commercial student, and to prepare bookkeeping sets in various lines of business that would illustrate the application of its principles.

I have found that in reclassifying accounts to conform with the theory and practice of accountancy, the art of bookkeeping has been made easier to learn and easier to teach, rather than more difficult. True science simplifies any subject of which it treats, and accountancy is the true science of bookkeeping.

Five distinct subjects are included:—the fundamental and elementary principles of accountancy, the art of bookkeeping as applied in various lines of business, business methods and practices, office methods and practices, and office appliances.

The following are some of the features of particular interest:

1. For students who are beginning, teachers can have their choice of (1) the account, or skeleton ledger method, (2) the theory method, using transactions stated in the form of memorandums, or (3) the illustrated theory method, in which the business papers received and issued are used in connection with the printed text, either for purely illustrative purposes, or as data from which records are to be made in the various books. The subject matter is the same, except that it is presented in different order in each method.

2. The transactions are classified and entered in the books in which they properly belong, from the start. Purchases, sales, notes and acceptances, cash receipts and payments, etc., are entered directly in their respective books, from which the proper accounts in the ledger are debited and credited.

3. Various price lists are provided with each set, which may be used, if desired.

4. Business practice with offices may be conducted with each set, if desired.

5. The transactions of each set are confined to those usually found in the particular line of business illustrated. All unnecessary and unbusinesslike transactions are omitted.

6. The transactions of each set and the accounts growing out of them are classified according to the principles and rules of modern accountancy.

7. The business methods commonly followed in the various lines of business illustrated in the different sets are fully explained in connection with the transactions to which they apply.

8. The trading and profit and loss statements, statements of resources and liabilities, and the other statements, analysis sheets, etc., required in connection with each set conform strictly to the established forms of these statements employed by accountants.

9. The business papers and forms are selections from the best lithography produced, many of them showing unique and practical ideas in design and arrangement to facilitate and safeguard business transactions.

10. Ledger closings, the grouping of accounts, the use of controlling accounts, the analysis of accounts, and the preparation of various supplementary and supporting statements are given special attention and thorough treatment.

11. Manufacturing accounts and statements, corporation accounts, the voucher system of accounts, branch store, agency, and other special accounts are fully explained and illustrated.

12. Cost accounting, cost records and systems are given ample treatment for the elementary student.

13. The principles, rules and practices of accountancy are fully set forth in a separate chapter.

14. Office systems and appliances are explained and illustrated in a separate chapter, with incidental reference to their use at various points in the different sets.

15. Supplementary drills, that feature which proved to be so valuable in my older bookkeeping publications, are provided wherever needed.

I wish to acknowledge the valuable services rendered in the preparation of manuscript and the reading of the proof by my good friend, B. P. Leister, C.P.A., a former pupil, who was for many years a most successful teacher of the commercial branches, and who is now in full practice as a certified public accountant. I also wish to acknowledge my obligation to the many other accountants who have assisted me in various ways in the preparation of this book, and who have responded so freely to my requests for suggestions and criticisms.

The Author.

BALTIMORE, MD.
June 10, 1910.

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BOOKKEEPING AND ACCOUNTANCY

1. Bookkeeping. The art of classifying and recording business transactions and facts systematically is called *bookkeeping.*

2. Accountancy is that branch of practical science which treats of the *methods* of classifying and recording business transactions and accounts so that the facts they exhibit shall be shown in their proper relations, expressed in terms that will most fully provide the information necessary to successful business and financial administration.

3. A business transaction is an *exchange* of something for something between persons; that is, one person *receives* something of value from another for which he *gives* something of equivalent value in exchange.

4. Value is represented in anything that has *worth, purchasing power,* or *utility,* such as property, merchandise, money, uses, and services.

5. As to the time of transfer by each party, transactions are of two kinds, *completed* and *uncompleted.*

6. A completed transaction is one in which the exchange of value is made by both parties *at the same time.*

7. An uncompleted transaction is one in which the transfer is made by one party but not by the other, the transfer by the second party being made *at some future time.* Such a transfer is said to be "on account."

8. An uncompleted transaction is completed when the transfer by the second party is made to the first, the transfer by the first party having been made *at some previous time.* Such a transfer is said to be "on account."

9. During the interval of time between the transfer by the first party and the transfer in payment by the second party, which interval of time is known as the "term of credit," the second party *owes* or is *in debt* to the first party and the first party *trusts* or *gives credit* to the second party, therefore,—

10. A **debtor** is one who *owes* or is *in debt* or has been trusted, and the amount he owes is known as a *debit* in the account kept with him by the creditor. He is the *receiver* of something of value for which he does not *at that time* give value.

11. A **creditor** is one who is *owed* or has *given credit* or trust, and the amount that is owed to him is known as a *credit* in the account kept with him by the debtor. He is the *giver* of value for which he does not *at that time* receive value.

12. An important distinction. The words "debtor" and "creditor" refer *only to persons*, and, in the sense of owing or being owed, debit and credit *can only be used in connection with personal accounts.* Debit and credit as applied to all other accounts are used only as convenient terms to designate *which side* of the account is referred to, and do not imply that the things represented by these accounts owe or are owed.

13. Things represented by impersonal accounts cannot owe or be owed, although some writers erroneously personify them so as to apply the principles of debit and credit relating to personal accounts. This can never be done, however, without violating the simplest principles of logic and reason. Merchandise could not owe or be owed, since *it belongs to the owner* and is in his possession. Merchandise accounts show the *costs of purchases* and the *returns from sales.* Likewise cash is in the possession of the owner, and cash account shows *receipts* on one side and *payments* on the other. The various expense items show what the expenses of the business cost, i. e., the outlays necessary to earn the incomes of the business as shown in the various income accounts. The only reason for using the terms "Dr." and "Cr." to designate the two sides of impersonal accounts is because they are the most *convenient* and the briefest terms that can be used.

14. A **creditor trusts** or gives credit to a debtor because of an expressed or implied *promise* or *contract* on the part of the debtor to pay the creditor at some future time. When expressed, the promise or contract may be made *orally*, i. e., "by word of mouth," or in *writing.* When in writing it becomes a "written promise to pay," and is usually in the form of a *promissory note* or of an *acceptance.*

15. An oral promise or contract to pay may afterwards be changed into a *written* promise or contract to pay, in the form of a promissory note, accepted draft, or other written obligation.

ACCOUNTS

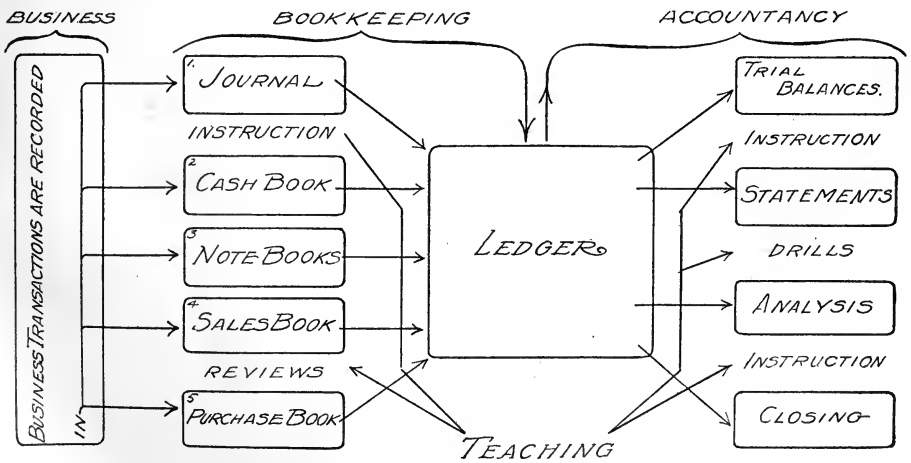
16. An account is a record of one or more items relating to the same *person* or *thing*, kept under an appropriate heading or title. It is the custom to place the debit items on the *left-hand* side and the credit items on the *right-hand* side of the accounts in the ledger. Accounts show similar items arranged in the most convenient form for *arithmetical solution and analysis.* They are divided into several classes depending upon their purpose and the results they show. The following is the standard form of a ledger account.

LEDGER ACCOUNTS

Year Month	Day	Explanation	Page	Dollars	Cents	Year Month	Day	Explanation	Page	Dollars	Cents
		(When used, but frequently omitted)	of book containing original entry					(When used, but frequently omitted)	of book containing original entry		

17. The Ledger is the book of accounts. The debit and credit items arising from the various kinds of transactions are transferred from the different books in which the transactions are classified and recorded to the proper accounts in the ledger. These books are the cash book, sales book, purchase book, journal, notes receivable and notes payable books, and such other books as may be required, depending upon the nature and extent of the business. These are known as *books of original entry.*

17*a*. A GRAPHIC ILLUSTRATION OF THE COURSE OF TRANSACTIONS, AND THE RELATIONS OF BUSINESS AND TEACHING TO THE SUBJECTS OF BOOKKEEPING AND ACCOUNTING.



DEBITING AND CREDITING ACCOUNTS

18. To determine what accounts are to be debited and what accounts are to be credited in any transaction we apply the *laws of debits and credits* which are expressed in *rules of bookkeeping.* They are derived from the customs and practices of business men, and conform with the principles of accountancy.

19. A law is a statement of a principle. It is a rule of action.

20. In every transaction there are one or more debit items and one or more credit items.

21. Debit and credit items are of three kinds, (a) those relating to *personal* accounts, (b) those relating to accounts with *cash, notes, acceptances,* and other mediums of exchange, and (c) those relating to accounts with *property,* with *uses,* with *services,* with *allowances,* with *expenses,* and with *incomes* and *revenues.*

22. Debit and credit items relating to accounts with *persons* invariably show that each person debited is the *receiver* of something of value without *at that time* giving value in return, and that each person credited is the *giver* of something of value without *at that time* receiving value in return. (¶10 and 11.) Such items usually relate to "uncompleted transactions." (¶7 and 8.)

22*a*. Remember that the "*receiver*" is the party who receives something of value from us *without at that time giving value in return.*

22*b*. Remember that the "*giver*" is the party who gives something of value to us *without at that time receiving value in return.*

23. Debit and credit items relating to accounts with *cash, notes, acceptances* and other *mediums of exchange,* invariably show that each account is debited for the face value of *what is received* (or redeemed), and that each account is credited for the face value of *what is given* (paid, issued, or parted with). The principal accounts of this kind are cash account, notes receivable account and notes payable account.

24. Debit and credit items relating to accounts with *property, uses, services, allowances, expenses, incomes,* etc., invariably show that each account is debited for the *cost* of what is represented by the account, and that each account is credited for *returns* from what is represented by the account. The principal accounts of this kind are those relating to the purchase and sale of merchandise, real estate and buildings, stocks and bonds, furniture, fixtures, and other forms of property and investments of capital, and those showing the expenses and incomes such as interest, discount, commission, merchandise discounts, freight and express charges, rent, insurance, taxes, wages, salaries, and all other accounts showing the sources of the losses and the gains of the business.

CLASSIFICATION OF DEBIT AND CREDIT ITEMS.

25. Notice that in debiting accounts as stated in the preceding paragraphs, 22, 23 and 24, in every instance in debiting a personal account *the receiver* is debited; in debiting cash, notes receivable and notes payable accounts, they are debited for *what is received;* and in debiting all other accounts they are debited for the *cost* of something of value received.

26. Notice that in crediting accounts as stated in the preceding paragraphs 22, 23 and 24, in every instance in crediting a personal account *the giver* is credited; in crediting cash, notes receivable and notes payable accounts, they are credited for *what is given;* and in crediting all other accounts they are credited for the *returns* from something of value given.

27. From the classification of items, as given in paragraphs 25 and 26, the following simple rule for debiting and crediting the proper accounts for all items growing out of the current transactions of business is derived.

GENERAL RULE FOR DEBITING AND CREDITING ACCOUNTS.

28. *Debit the Receiver, what is received, and that which costs value.*

29. *Credit the Giver, what is given, and that which returns value.*

30. The various applications of this general rule to all kinds of business transactions will be shown under the different accounts, explained on the following pages.

PERSONAL ACCOUNTS.

31. These are accounts with individuals, firms, and corporations (persons), which are required in "uncompleted transactions," or those transactions "in which the transfer is made *at that time* by one party but not by the other." (¶7 and 8) Such transactions are said to be "on account."

32. The object is to ascertain *what others owe to us* on account or *what we owe to others* on account "during the interval of time between the transfer by the first party and the transfer in payment by the second party." (¶9) During the "interval of time," if a personal account shows an amount owing to us, it is a *resource* (¶461); if it shows an amount owing to others, it is a *liability.* (¶462)

Rule for Debiting and Crediting Personal Accounts.

33. *Debit the receiver: credit the giver.*

34*a* Debit **the receiver** in the proper account.

34*b*. Credit **the giver** in the proper account.

35. The *various applications* of the rule for debiting and crediting personal accounts are as follows:

(*Not to be memorized. To be used only as called for.*)

36. Debit *persons* in their accounts,

a. For the amount they owe us at the beginning of business.

b. For all goods or property sold to them on account.

c. For all money paid or loaned to them on account, or paid by us to others at their request.

d. For all goods, etc., we return to them for which we have previously credited them.

e. For all notes made by us (notes payable) and given to them on account.

f. For notes and acceptances of others (notes receivable) transferred by us to them on account.

g. For all drafts drawn by them and accepted or paid by us on account.

h. For our drafts or orders on others drawn (or indorsed) by us in their favor on account.

i. For discounts or other allowances made to us on account.

j. For "shortage," "damage," or "overcharge" claims they allow to us on goods for which we have previously credited them.

k. For freight or express charges paid by us when goods are purchased from them f. o. b. *delivery point*, or when goods are sold to them f. o. b. *shipping point*.

l. For the amount "thrown off" a debt when they agree to accept a part of what we owe them in full satisfaction of the debt.

---

38 **Observe** that in every instance the party debited is the *receiver* of something of value *from* us without at that time giving value in return: hence the rule.

37. Credit *persons* in their accounts,

m. For the amount we owe them at the beginning of business.

n. For all goods or property bought from them on account.

o. For all checks, money or other cash received from them on account, or paid by them to others at our request.

p. For all goods, etc., they return to us for which we have previously debited them.

q. For all notes made by them and given to us (notes receivable) on account.

r. For notes and acceptances of others (including our own notes, etc.,) transferred by them to us on account.

s. For drafts drawn on them by us on account.

t. For their drafts on others drawn (or endorsed) by them in our favor on account.

u. For discounts or other allowances made to them on account.

v. For "shortage" "damage," or "overcharge" claims allowed to them on goods for which they have previously been debited.

w. For freight or express charges when paid by them on goods purchased from them f. o. b. *shipping point*, or when goods are sold to them f. o. b. *delivery point*.

x. For the amount lost by us when we agree to accept a part of what they owe us in full satisfaction of the debt, or when the account is uncollectable.

---

39 **Observe** that in every instance the party credited is the *giver* of something of value *to* us without at that time receiving value in return: hence the rule.

Note to the teacher and student: The *various applications* stated under each account are not to be memorized, but are intended to *assist the student in applying the rule.* As they are applied to transactions, they should be carefully studied until their relation to the rule is clearly understood.

40. Transactions Illustrating the Various Applications of the Rule (33) for Debiting and Crediting Personal Accounts.

Transactions with R. J. Maclean & Co., 912 Wabash Ave., Chicago, Ill.

(The paragraph numbers in brackets refer to the *various applications* of the rule for debiting and crediting personal accounts.)

Jan. 1. They owe us on account, at the beginning of business, $112.50. (¶36*a*) -- Jan. 3. Sold them merchandise on account, $975. (¶36*b*) -- Jan. 5. Received cash on account $100. (¶37*o*) -- Jan. 6. Bought merchandise on account, $316.50. (37*n*) -- Jan. 7. Paid them cash to apply on bill of Jan. 6, $56.50. (¶36*c*) -- Jan. 7. They returned for credit goods ordered by mistake on Jan. 3, amounting to $7.75. (¶37*p*) -- Jan. 9. Received their note at 30 days to apply on bill of Jan. 3, $125. (¶37*q*) -- Jan. 10. We returned to them for credit goods purchased Jan. 6, amounting to $12.60. (¶36*d*) -- Jan. 11. We gave them our note at 60 days, on account of bill purchased Jan. 6, $50. (¶36*e*) -- Jan. 11. Received from them, to apply on account, Jones & Co's note, which they transferred to us by endorsement, for $37.50. (¶37*r*) -- Jan. 12. We have drawn a draft at 10-days sight on them on account, in favor of Charles Adams, for $75. (¶37*s*) -- Jan. 13. Received from them, to apply on account, their draft at 5 days sight on Alex. King & Co., Cleveland, O., drawn in our favor, for $91.61. (¶37*t*) -- Jan. 14. We accepted their draft at 10 days' sight drawn on us, to apply on account of bill purchased Jan. 6, in favor of Harris Grocery Co., for $23.46. (¶36*g*). On the same day we transferred to them, by endorsement, to apply on account of the same purchase, A. S. Baird & Co.'s note in our favor for $45. (¶36*f*) -- Jan. 16. They report short weight in flour sold them of Jan. 3, amounting to $4.50, which we allow. (¶37*v*) -- Jan. 16. We prepaid freight charges on goods sold to them on Jan. 3, for their account, $2.20. (¶36*k*) -- Jan. 17. We allow them a discount of 1% on bill purchased Jan. 3, $9.75. (¶37*u*) -- Jan. 17. They allow us a discount of 2% on bill of Jan. 6, $6. 33. (¶36*i*) -- Jan. 19. They have allowed us an overcharge claim which we made on their bill of Jan. 6, for $2.41. (¶36*j*) -- Jan. 19. We drew a draft at 5 days' sight in their favor, in full for their bill of Jan. 6, on H. S. Gray & Sons, for $120.20. (¶36*h*) -- Jan. 20. They forwarded us a receipted freight bill for $1.65, which was paid by them on goods shipped Jan. 3, which were to be shipped f. o. b. delivery point. (¶37*w*) -- Jan. 21. They have offered to give us a check of $110 in full payment of the amount owed us on account, Jan. 1, which we have accepted. (¶37*o*). -- The amount lost is $2.50. (¶37*x*) -- Jan. 30. Received from them, on account, John G. Taylor's acceptance for $150 (¶37*r*) and their check for $75 (¶37*o*).

What is the balance of account January 31?

EXERCISE.

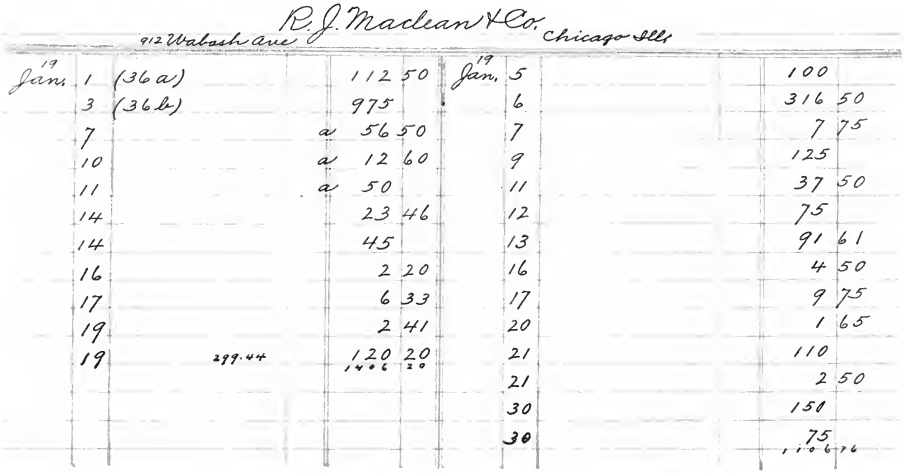
40*a*. Prepare a ledger account for the above transactions on ledger paper, as follows: (*If you do not have ledger paper, rule the form of a ledger page on blank paper.*)

(1) Read and study each transaction carefully.

(2) Read the special application, for each transaction, of the rule for debiting and crediting personal accounts, indicated by the paragraph number.

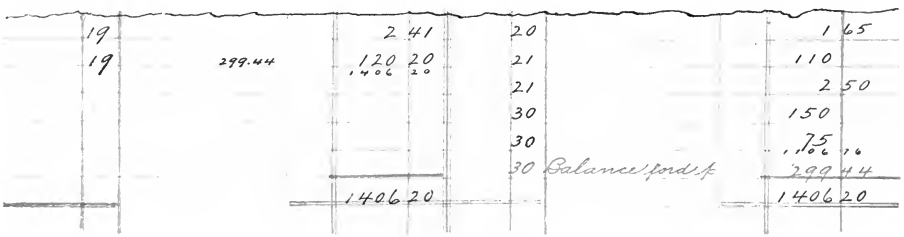
(3) Apply the rule (33) and make the proper debit or credit entries in the account, as shown in the illustration (1). When completed, submit for approval.

ILLUSTRATION 1.



40*b*. *The illustration* shows the ledger account as it appears at the end of the month, January 31, with the figures in the posting columns omitted. The *small* figures showing the footings of each column and the balance of the account, $299.44, are *pencil* figures, written when the account is footed, preparatory to taking the trial balance. If it is desired to close the account for either of the reasons stated in ¶44, the account would be ruled and footed, as shown in illustration 2. (¶45)

ILLUSTRATION 2.



40*c*. *Indicating canceling items.* When payments are to be applied to a particular bill, the canceling items may be indicated by letters used in the order of the alphabet as each item is posted. (¶46*c*) The same method applies when the balance of the bill is to be determined or paid, or when the account is to be analyzed. Notice that in the transactions for the account of R. J. Maclean & Co. (¶40), the second transaction of January 19 states that the amount is "in full for their bill of Jan. 6;" consequently, the sum of the items received to apply in payment of tnat bill should equal and *cancel* the amount of the bill. The first three of the canceling items of the purchase of Jan. 6, on the debit side of the account, are indicated by the letter "a" in the illustration.

40*d*. *Begin with the transaction of Jan. 7*, and place the letter "*a*" opposite each item in the account you have just prepared on the double line opposite the amount. If the sum of these items equals the total amount of the bill, $316.50, place the letter "*a*" opposite that amount. In like manner, indicate the items on the credit side of the account, canceling the debit item of Jan. 1, for $112.50, by inserting the letter "b" on the double line opposite the amounts on each side of the account.

This method of indicating canceling items illustrates a very common practice in proving or analyzing accounts. This is a *mixed* account. (¶51)

To Close Personal Accounts.

41. The object is to ascertain the amount owed *to* us by each person or *by* us to each person having an open account on our books.

42. The difference between the two sides of a personal account (if any) will show the amount owed to us or by us. If the *debit* side is the larger it will show the amount (balance) owed to us, which is a *resource.* (¶461) If the *credit* side is the larger it will show the amount (balance) owed by us, which is a *liability.* (¶462.) In either case the balance should appear as an item in the statement of resources and liabilities (¶487), or in the balance shown by the "accounts receivable" or "accounts payable" accounts in that statement.

43. *The difference shown by a personal account is always a balance,* but if the balance is uncollectable, then it shows a *loss.* When a personal account is considered of doubtful value, or if any part of it is likely to be uncollectable, it may be closed into a "doubtful accounts" account until such time as it is found to be positively uncollectable, when it should be considered as a loss.

44. To close. Personal accounts should never be closed unless they are paid in full and, consequently, balance themselves, except in the following cases:

(*a*) when an adjustment of the account has been made and the correct balance determined, when it may be ruled up and the balance brought down to begin a new account, (*b*) when the space allotted is filled and it is necessary to forward the account to another page, or to a new ledger, when the *balance only* should be forwarded, and (*c*) when the party becomes insolvent and the account is uncollectable, when it should be closed into "bad debts" account or, if there are few such entries, directly into the profit and loss account.

Ruling Personal Accounts.

45. The proper ruling for a personal account depends somewhat upon the nature of the business transacted, and more particularly upon the method followed in the payment of bills. In this respect, personal accounts may be divided into four classes, (*a*) those accounts in which each item or bill is paid separately, (*b*) those accounts where several items or bills are paid at one time, (*c*) those accounts where one item or bill is paid in two or more payments, and (*d*) those accounts where payments are made "on account" but not in full settlement of any particular item or bill, which are known as "running accounts." Any one or more of these various methods of payment may be shown in a single account, and the account may be either an account receivable or an account payable. (¶49 and ¶50.)

46. The following accounts illustrate the various methods of payment referred to and the proper rulings for each.

Illustration 3.

Park Grocery Co. 33 Elm St.

19				19			
Mar.	6	Mdse	34 40	Mar.	16	Cash	34 40
	12	"	109 48		23	"	109 48
	15	"	68 19		30	"	68 19
	25	"	16 45	Apr.	7	"	145 32
	29	"	128 87				
Apr.	5	"	83 37				
	24	"	12 21				

46*a*. *Explanation.* This account belongs to the class described in ¶45*a* and ¶45*b*. It shows that the item debited March 6 was paid March 16, that the item debited March 12 was paid March 23, and that the item debited March 15 was paid March 30. The items of March 25 and 29 were paid April 7 in one amount. The red lines were ruled underneath the balancing items as each credit entry was made. The items of April 5 and 24 are unpaid, and their sum, shown in pencil figures, is the balance of the account. This is an *account receivable.* (¶49)

ILLUSTRATION 4

Dodge Electrical Supply Co. 139 Water St. Pittsburg Pa.

19				19			
Sep.	5	Cash	45 95	Aug.	12	Mdse	12 98
					16	"	23 36
					25	"	9 61 (45 95)
				Sep.	3	"	43 18
					30	"	11 90 (55 08)

46*b*. *Explanation.* The items of August 12, 16 and 25 are for purchases which were paid in one amount September 5, at which time the red lines were ruled under the balancing items. The pencil footing on the credit side shows the balance of the account September 30. This is an *account payable.* (¶50) It illustrates the class of accounts described in ¶45*b*.

ILLUSTRATION 5

Gordon & Buchanan 371 Front St.

19					19			
Apr.	3	Mdse		a 216 50	Apr.	14	Cash	a 150
						19	"	a 66 50
	24	"		b 154 60		26	"	b 100
	27	"		b 31 77 (186 37)		27	"	b 50
	30	"		c 41 75		30	"	b 36 37 (186 37)
May	5	"		c 16 48	May	15	"	c 150
	12	"		c 141 41		25	"	c 89 14 (239 14)
	22	"		c 39 50 (239 14)		29	"	100
	26	"		106 20				
	28	"	13.42	7 22 (113 42)				

46*c*. *Explanation* An examination of the entries in this account in the order of their dates will explain the rulings shown. It is an *account receivable* and illustrates the practice of many bookkeepers. It will be noticed that when all items balance above a given point they are ruled out, as shown by those marked "*a*," "*b*" and "*c*," whether they are on the same line or not. The letters also show the method of indicating canceling items. The balance is found by taking the difference between the two sides of the account, as shown in the small pencil figures in the left hand explanation column.

Exercises in Personal Accounts.

47. Prepare the ledger accounts for the following examples, applying the rule (¶33) to each transaction. If you do not have ledger paper, rule the form of a ledger on blank paper. Enter the amount *first*, then the date. As each entry is made, insert the paragraph number and letter of the particular application of the rule for debiting and crediting personal accounts (¶36 and ¶37) which applies, as shown in brackets for the first two items in illustration 1. Rule out the items that balance on each side of the account *as the balancing entries are made.* When the examples are completed, present them for approval.

(1.) Transactions with Robert G. Burns.

April 1. Sold him merchandise on account, $45. (¶36*b*) · April 4. Sold him merchandise on account, $16. – – April 10. Received cash from him for bill sold April 1, $45. (*Rule out balancing items* ($45) *on each side of the account as shown in the illustration 3.*) – – April 13. Sold him merchandise on account, $21. – – April 18. Sold him merchandise on account, $73. – – April 19. Received cash for bill sold April 4, $16. (*Rule out balancing items.*) – – April 24. Sold him merchandise on account, $15. – – April 25. Received cash from him for bill sold April 18, $73. – – April 27. Received cash from him for bill sold April 13, $21. (*Rule out balancing items.*) – – April 28. Sold him merchandise on account, $18. What is the balance shown by the account? What method of paying bills is shown by this account? (¶45*a*)

(2.) Transactions with Miller Brothers.

May 1. We owe them on account, at the beginning of business, $115.25. May 3. Bought goods from them on account, $73.12. – – May 4. Paid them cash in full of account to date, $188.37. (*Rule out the balancing items on the same line.*) – – May 6. Bought goods from them on account, $87.50. – – May 8. Bought goods from them on account, $17.94. – – May 9. Gave them our note at 30 days in payment of bills of May 6 and 8, $105.44. (*Rule out balancing items.*) – – May 12. Bought goods from them on account, $236.20. – – May 14. Bought goods on account, $36.12. – – May 15. Returned goods included in bill purchased May 12, $13.75. – – May 16. Bought goods from them on account $327.45. – – May 17. Paid them in full for bills of May 12 and 14, $258.57 (*Rule out balancing items.*) – – May 17. Paid freight on goods purchased May 16, which were to be prepaid to delivery point by Miller Brothers, $4.50. What is the balance shown by the account, and who owes the balance, we or Miller Brothers? What method of paying bills is shown by this account? (¶45*b*) Does this account show a resource or a liability? (¶42) Is this an account receivable or an account payable? (¶50)

(3.) Transactions with Murphy & Morgan.

June 1. Sold them goods on account, $256.95. – – June 3. Received cash to apply on bill of June 1, $150. – – June 4. Received cash in full for bill of June 1, $106.95. (*Rule out balancing items.*) – – June 6. Sold them goods on account $342.36. – – June 10. They returned goods amounting to $7.80. – – June 11. Received their note in our favor at 30 days in part payment of bill of June 6, $180.

– – JUNE 12. They transferred to us, on account, a note made by Marshall & Company, in their favor for $100. – – JUNE 12. Received cash in full of bill of June 6, $54.56. (*Rule out balancing items.*) – – JUNE 24. Sold them goods on account, $96.36. – – JUNE 29. We allowed them an overcharge claim on goods sold on June 24, $3.60. – – JUNE 30. Sold them merchandise on account, $23.50. – – JUNE 30. Received cash in full for bill sold June 24, $92.76. (*Rule out canceling items. It will be necessary to rule on different lines.*) (¶46*c*) What is the balance shown by the account? What method in the payment of bills is shown by this account? (¶45*c*) Is it an account receivable or an account payable? (¶49.)

(4) Transactions with Williams & Reynolds.

JAN. 1. At the beginning of business they owe us on account, $78.50. We owe them for an unpaid coal bill, $14.50. – – JAN. 4. Sold them goods on account, $668.70. – – JAN. 5. They return us goods amounting to $10.25. – – JAN. 8. Bought from them on account goods amounting to $463.61. – – JAN. 9. Received Hall & Co's acceptance in their favor, which they have transferred to us on account, $55.30. – – JAN. 10. We allow their claim of $1.36 for an overcharge on goods sold them Jan. 4. – – JAN. 10. Accepted their draft at 10 days' sight, on account of bill of Jan. 8, $165. – – JAN. 12. Allowed them a discount of 1% on bill sold them Jan. 4, $6.69. – – JAN. 14. We transferred to them, on account of bill of Jan. 8, F. C. Archer's acceptance in our favor, $132.50. – – JAN. 15. We made draft on Miller Brothers, in their favor, on account of bill of Jan. 8, for $100. – – JAN. 15. They allowed us a discount on bill purchased Jan. 8, $9.37. – – JAN. 17. We paid them balance due on bill purchased Jan. 8, $56.74. (*The items canceling the bill purchased Jan. 8 may be indicated in the account, as instructed in ¶40c and ¶46c.*) – – JAN. 18. Received cash in payment of amount due us Jan. 1, $78.50. (*Check canceling items as instructed for the preceding transaction.*) – – JAN. 19. Received their draft on Perkins Brothers, in our favor, on account, $350. – – JAN. 19. Paid them in settlement of coal bill owed to them Jan. 1, $14.50. (*Check canceling items.*) (¶40*c* and 46*c*) – – JAN. 21. They desire to settle their account. What is the balance shown by the account? Is this an account receivable, an account payable, or a mixed account? (¶51) As it stands, Jan. 21, to which group does it belong?

(5) Transactions with Rodney, Gates & Co.

(Note that these are *our* transactions with them, not theirs with us.)

SEPT. 1. Bought merchandise on account, $128.15. – – SEPT. 3. Bought merchandise on account, $216.45. – – SEPT. 4. By paying cash, we are entitled to a discount of 2% on bill of Sept. 1, $2.56. (¶36*i*) We paid them the balance in cash, $125.59. (¶36*c*) (*Check canceling items as instructed in ¶40c in this and other transactions in this account.*) – – SEPT. 10. Bought merchandise on account, $33.62. – – SEPT. 12. Bought merchandise, $92.18. – – SEPT. 14. Deducted 2% discount on bill of Sept. 12, $1.84. Paid balance of the bill in cash, $90.34. (*Check canceling items.*) — SEPT. 15. Accepted draft at 30 days in payment of bill of Sept 10, for $33.62. – – SEPT. 17. We are allowed an overcharge claim on bill of Sept. 3 for $4.16. We give our note at 60 days for the balance, $212.29. – – SEPT. 20. We have paid a freight bill on goods received Sept. 3, which should have been prepaid by Rodney, Gates & Co., $9.41. What is the balance shown by the

account? Is it a resource or a liability? What method was followed in the payment of bills in this account? As it stands, is it an account receivable or an account payable? Ordinarily, to which group of accounts would it belong?

(6) Transactions with Morrell Mfg. Co.

Nov. 1. Sold them a milling machine, on account, $340. – – Nov. 20. Bought from them 1 Acme forge, $72.50. – – Nov. 21. Paid them cash in full for the Acme forge, $69.60, they allowing us a 4% discount on the bill, or $2.90. (*Check canceling items.*) – – Nov. 26. Received their draft on King's Sons, drawn in their favor and endorsed by them to us, in payment of bill sold Nov. 1, $340. – – Nov. 29. Received cash from them as a deposit, in part payment of 1 "Hanover" lathe No. 3, not yet delivered to them, $150. – – Nov. 30. Shipped them 1 No. 3 "Hanover" lathe, as per contract, $490. What is the balance of the account? To what class of accounts does this account belong?

(7) Transactions with S. R. Brown.

Dec. 10. Loaned him cash, $75, which he returned in payments as follows: Dec. 20, $10; Dec. 23, $20; Dec. 27, $30; Dec. 30, $10. Does the balance of the account show a resource or a liability? How does the account differ from an ordinary account receivable or account payable? (¶51)

Grouping Personal Accounts.

48. For accounting purposes, and particularly to provide a convenient arrangement of the accounts in the ledger, personal accounts are divided into two groups known as *accounts receivable* and *accounts payable.*

49. Accounts receivable are the accounts with persons to whom we sell, and usually show debit balances (if any) which are *resources* or assets. The sum of those balances shows the amount owing from accounts receivable, which should be included as a resource item in the statement of resources and liabilities. (Illustration 93)

Illustration 6.

Statement of accounts receivable January 31, 19

R. J. Maclean & Co.	299 44	
John B. Simpson	316 49	
Archer & Lane	721 16	
H. R. Warner & Co.	1477 28	
Billings Supply Co.	19 46	
E. F. Fairchild & Sons	833 67	3667 50

Notice that the sum of these balances equals the balance shown by the accounts receivable account. (¶54)

50. Accounts payable are the accounts with persons from whom we buy, and usually show credit balances (if any) which are *liabilities*. The sum of these balances shows the total amount owing on accounts payable, which should be included as a liability item in the statement of resources and liabilities. (Illustration 93.)

ILLUSTRATION 7.

Statement of accounts payable January 31, 19

Henry G. Stebbins & Co.	1346	78	
John Willington	936	60	
Channing & Co.	2243	84	4527 22

Notice that the sum of these balances equals the balance shown by the accounts payable account. (¶54.)

51. Personal accounts showing transactions outside of those usually relating to the purchase and sale of goods, which cannot properly be classed with either accounts receivable or accounts payable, are not infrequent. These are sometimes called *mixed* accounts, and usually appear as separate items, or in a separate group, in the trial balance. They may show either *resources* or *liabilities*, which in either case should be included in the statement of resources and liabilities. Again, goods may be purchased from and sold to the same party, and the account would, therefore, possess the characteristics of both an account receivable and an account payable. It is not unusual for separate accounts to be kept with the same person, one for purchases and one for sales, and in some systems of bookkeeping it is necessary.

52. When all the accounts of a business are kept in one ledger, it is preferable to group the accounts receivable in one section of the ledger and the accounts payable in another section of the ledger, reserving a third section for the general accounts.

53. When separate ledgers are kept for any one or more of these groups, they are usually designated as the *sales* or *customers* ledger for accounts receivable, the *purchase* ledger for accounts payable, and the *general* ledger for the general accounts. Where a private ledger is kept, it should contain the capital accounts of the owners and any other accounts which it is desired to keep private.

54. When separate purchase and sales ledgers are kept, it is customary to keep a *controlling* account for each ledger in the general ledger, to which is posted the totals of special columns in the various books of original entry in which are entered the items affecting the accounts in each ledger. The sum of the balances

in either ledger must equal the balance shown by the controlling account in the general ledger. (For fuller description, read ¶566)

54*a*. Illustrations 8 and 9 show the controlling accounts in the general ledger footed, closed, and the balances brought down. These accounts are usually closed at the end of each fiscal period when the books are closed. It is from these accounts that the balances shown in the trial balance (¶483) are taken.

ILLUSTRATION 8

Accounts Receivable

19					19				
Jan.	1	Balance		317 39	Jan.	5	Mdse. rtd.	J	64 13
	31	Sales	3667 50 S	7107 20		17	Rebates & Allowances	J	35 14
						31	Cash	C	3657 82
						31	Balance		3667 50
				7424 59					7424 59
Feby.	1	Balance		3667 50					

ILLUSTRATION 9.

Accounts Payable

19					19				
Jan.	5	Mdse. rtd.	J	40 16	Jan.	1	Balance		2598 52
	16	Rebates & Allowances	J	17 40		31	Purchases	P	3184 03
	31	Cash	C	1197 77					
	31	Balance		4527 22					
				5782 55					5782 55
					Feby.	1	Balance		4527 22

54*b*. *In illustrations 8* and *9*, the letters "s," "j," "c," etc., which appear next to the single line to the left of the amount column on each side of the account, indicate the books from which the entries are posted. The letters representing the principal books kept in an ordinary set are, "p" for purchase book, "s" for sales book, "c" for cash book, "n" for note books, "j" for journal, etc. While the student is not required to enter these letters in the examples to be worked up under the various accounts, if they are noted by him it will assist him in understanding the books from which the various items are posted.

OWNERSHIP ACCOUNTS.

55. The owner or proprietor of a business may be an individual, a firm, or a corporation. When the owner is an individual, his investment or capital is kept in an account under his name, followed by the word "Capital," as, "Charles Graham, Capital." When two or more persons unite in conducting a business,

each contributing a part of the investment or capital, the union of capital and time, etc., is called a *firm* or *partnership*, and each partner's investment or capital is kept in an account under his name followed by the word "Partner," as, "O. B. Harvey, Partner." When the owner is a corporation, the investment or capital account is kept under a general title, such as "Capital Stock," etc., which is fully explained in the chapters devoted to corporations.

56. Two accounts. Usually the proprietor or each partner should have two accounts—a *capital* account showing his interest in the business, and a *personal* account. In the capital account only those items affecting the permanent investment of the owner should be recorded, while the personal account should contain the items growing out of his routine transactions, such as withdrawals of money for salary or on account, or of goods taken for private use, etc.

PROPRIETOR'S AND PARTNER'S CAPITAL ACCOUNTS.

57. These accounts, while widely different in their purpose, are kept much like ordinary personal accounts. They, however, are affected by the gains and losses resulting from and incidental to the business conducted, and, therefore, are not closed *until after the gains and losses have been ascertained.* They should be kept in the general ledger or in a private ledger

58. The object is to show the interest, equity, or ownership of the proprietor or partner in the business.

58*a*. There should be a distinction made between the *owner's* or *proprietor's capital* and the *business capital* of a concern. The former represents the interest or equity of the owner or proprietor *after all the debts of the concern have been paid,* which is shown by the difference between the total resources and the total liabilities, while the latter is represented by the total resources or possessions of the concern *including what is owing to the creditors.*

58*b*. The business capital of a concern is, therefore, made up of the *owners' capital,* and the *creditors' capital,* whose interest or equity is shown by the liabilities. If there are no creditors, there is no division of interest in the ownership. Creditors have the *first claim against resources,* and are given precedence over the claims of owners. For this reason, when the owner is a corporation it is not unusual to designate its obligations to its stockholders as *secondary liabilities.* Owners' claims, whether the ownership is vested in an individual, a firm, or a corporation, must be met from what remains of the resources after all other creditors have been satisfied. If the remaining resources are not sufficient to meet the owners' claims, *the shortage is the owners' loss.* Where the ownership is represented by partners or stockholders, the resources remaining after all other creditors are satisfied are distributed pro rata among them.

Rule for Debiting and Crediting Proprietor's and Partner's Capital Accounts.

59. *Debit the receiver: credit the giver.*

59*a*. Debit the **proprietor** or **partner** in his capital account for withdrawals from his capital investment.

59*b*. Credit the **proprietor** or **partner** in his capital account for his capital investment, or when he increases his capital investment.

60. The various applications of the rule for debiting and crediting capital accounts are as follows:

61. Debit the proprietor or partner in his capital account.

a. For what he owes to others at the beginning of business to be paid from the funds of the business.

b. For all withdrawals of money or property from the capital of the business.

c. For all his personal debts paid from his capital.

d. For the debit balance shown by his personal account, if it is to be deducted from his capital investment.

e. For his *net loss*, or that part of it which is to be deducted from his capital as shown by the profit and loss statement, or by the profit and loss account, when that account is closed.

62. Credit the proprietor or partner in his capital account.

f. For what he invests at the beginning of business as capital.

g. For his subsequent investments of capital.

h. For any debts of the busines paid by him from his private funds, as an additional investment of capital.

i. For the credit balance shown by his personal account, if it is to be added to his capital investment.

j. For his *net profit*, or that part of it which is to be added to his capital as shown by the profit and loss statement, or by the profit and loss account, when that account is closed.

63. Transactions Illustrating the Various Applications of the Rule for Debiting and Crediting Proprietor's and Partner's Capital Accounts.

Capital account of F. A. Raymond.

March 1. He invests $8000. (¶62*f*) He owes on a personal account to be paid from the funds of the business, $140. (¶61*a*) – – May 1. He adds to his capital investment, $5000. (¶62*g*) – – Sept. 1. He withdraws from his capital, $1500. (¶61*b*) – – Nov. 1. He pays a note, on which he had borrowed money that was used in the business, from his private funds, as an additional investment of capital, $6000. (¶62*h*) – – Dec. 1. His personal note for $100 is paid, which is to be deducted from his capital. (¶61*c*) – – Dec. 31. He is debited

for his net loss, as shown by the profit and loss statement, $453, at which time his account is closed, footed, and the balance brought down, showing a net capital of $16,807. (¶61*e*, 66) – – JAN. 12. He withdraws cash from his capital, $1000. – – JAN. 31. His personal account shows a debit balance of $200, which he wishes to be deducted from his capital account. (¶61*d*, 71*a*) – – JAN. 31. He is credited for his net profit, as shown by the profit and loss statement, $1202.46 (¶62*j*, 66) What is his net capital, January 31?

EXERCISE.

63*a* Prepare a ledger account for the above transactions on ledger paper, as follows:

(1) Read and study each transaction carefully.

(2) Read the special application for each transaction of the rule for debiting and crediting capital accounts, indicated by paragraph numbers.

(3) Apply the rule (59) and make the proper debit and credit entries in the account as shown in illustration 10. When completed, submit for approval.

ILLUSTRATION 10.

F. A. Raymond's Capital a/c.

19						19				
Mar.	1	Owed to others	J	140		Mar.	1	Investment	C	8000
Sept.	1	Withdrawn	C	1500		May	1	"	C	5000
Dec.	1	Personal note	C	100	1740	Nov.	1	"	11260	6000
	31	Net loss 10 mos.	J	453						19000
	31	Net Capital		16807						
				19000						19000
Jan.	12	Withdrawal	C	1000		Jan.	1	Net Capital	15607	16807
	31	Personal a/c	J	200			31	Net profit 1 mo.	J	1202 46
	31	Net Capital		16809 46						
				18009 46						18009 46
						Feby.	1	Net Capital		16809 46

63*b* The illustration shows the account as it appears at the end of the month. The figures are omitted from the posting columns. The small pencil figures showing the footings of each column and the balance of the account are written when the account is footed preparatory to taking the trial balance. The account is balanced, ruled, and the balance brought down after the net profit for the year and the balance shown by the proprietor's personal account are posted from the closing entries in the journal.

To Close Proprietor's or Partner's Capital Account.

64. **The object** is to ascertain the amount of his net capital or net insolvency *at a certain date.*

65. **The difference** between the two sides of a capital account, after the net profit or the net loss of the proprietor or partner and any other accounts affecting it have been closed into it, shows the proprietor's or partner's net capital or net insolvency, (a) *net capital* when the credit side is the larger, (b) *net insolvency* when the debit side is the larger. In either case they should be shown in a separate section of the statement of resources and liabilities, which is the last section of that statement.

66. **To close.**—After the net profit or the net loss is posted from the closing entry in the journal, if the credit side is the larger, enter on the debit side in red ink, (1) the amount of the difference, (2) the date of closing, and (3) the words "Net Capital" or "Balance." Then rule the account as shown in illustration 10, and bring down the balance (in black ink) on the opposite side, entering the date of the next business day. (See second closing.)

67. *If the debit side is the larger,* enter the difference on the credit side using the words "Net Insolvency" or "Balance." After the account is ruled and footed the amount is brought down on the debit side of the account.

Exercises in Proprietor's and Partner's Capital Accounts.

68. Prepare ledger accounts for the following examples. As each entry is made, insert the paragraph number and letter of the particular application of the rule for debiting and crediting capital accounts which applies. Foot, balance and rule up the accounts and bring down the balance when so instructed.

(1) Capital account of Henry B. Walters.

Jan. 1. He invested $5,000. (¶62*f*) – – July 1. He invested $2,000. – – Oct. 1. He drew out $800. (¶61*b*). What was the balance shown by his account at the close of the year, Dec. 31, at the time of taking the trial balance?

Dec. 31. When the profit and loss statement was made out for the year's business, it was found that his net gain was $1,275. (¶62*j*) What was his net capital? Show the account ruled and closed, as illustrated in example.

(2) Capital account of George Henderson.

Jan. 1. He invested $10,000. – – Jan. 1. He owed to others to be paid from the funds of the business, $1,150. – – Feb. 1. He invested an additional $3,000. – – April 1. He withdrew from his investment, $1,000. – – July 1. He pur-

chased a warehouse and lot for his business, for which he paid from his private funds as an additional investment of capital, $4,000. (¶62*h*) – – DEC. 31. At the close of the year's business his profit and loss statement showed a net profit for the year of $4,250. (¶62*j*) What was his net capital at the beginning of the second year's business?

(3) Capital account of Charles E. Ford, Partner

JAN. 1. He invested $26,700. He owed on notes, which were assumed by the firm, $1,700. – – JUNE 10. He purchased an automobile, for which the firm's check was given, to be deducted from his capital, $1,600. – – JUNE 30. His net loss for the half year, as shown by the profit and loss statement, was $790. Prepare the account showing his net capital June 30, with the account properly ruled and footed. – – JULY 15. He paid from his private funds the firm's note for $3,000 as an additional investment. – – SEPT. 1. He withdrew from his capital invested, $1,000. – – DEC. 31. His net gain was shown to be $7,450. Show his net capital Jan. 1, with the account properly footed and ruled.

THE RELATIONSHIP BETWEEN THE OWNER AND THE BUSINESS.

69. Many authors have adopted the plan of *personifying the business*, whether it be the business of an individual, a firm, or a corporation, not only in formulating rules for capital accounts, such as "Credit the proprietor for what *the business* receives," but for the general accounts as well; hence we see such rules as "Debit what *the business* receives," "Credit what *the business* disposes of," "Debit cash for all cash *the business* receives," "Debit expense for all expenses of *the business*," etc. These and many similar statements set up the theory that a business is an *active personality* with power to receive and dispose of—to do or not to do; but this theory is illogical and untenable, because a business is merely the creation of the parties who own, control, manage, and conduct it, whether they are real or fictitious (corporate) persons. It has power of itself to do nothing. It could not exist without an owner. Only the owner can sue or be sued. Therefore, *this theory is not recognized in this work.*

69*a*. **The only purely personal relation** established in connection with any business is between the owner (represented in the real or fictitious persons conducting it) and the persons who deal with the owner, which is the usual relation of debtor and creditor. (¶11 and ¶12.)

69*b*. **There is, however, a semi-personal relation** established between the owner and the business itself, but it is a relation between the owner and something which is not or could not be a debtor or a creditor. While the owner is credited in his capital account for what he puts into the business, the business does not become *indebted* to him in any way, nor is his investment considered as a liability of the business, because he *owns* the business and its success or failure rests with him. If he withdraws from the capital, he is debited in his capital account, not that he owes anything, but because he, as the owner, is *charged back* with something that he formerly put into the business or that he has earned in conducting the business. The same is true of the owner in a corporation, although the earnings pass to the stockholders through a dividend instead of through the capital account.

PROPRIETOR'S AND PARTNER'S PERSONAL ACCOUNTS.

70. The personal account of a proprietor or partner is treated like any other personal account. It is indicated by adding the word "Personal" in the heading. It is opened for the purpose of keeping incidental items, such as withdrawals on account of salary, etc., separate from the items entered in the more permanent capital account.

71. The personal account of a proprietor or partner is debited (*a*) for all sums withdrawn for private use which are not to be deducted from the capital investment, (*b*) for any personal debts paid or to be paid from the funds of the business, (*c*) for all sums collected from customers and retained by the proprietor or partner. It is credited (*d*) for any sums paid in subject to immediate withdrawal, (*e*) for any debts of the business paid from private funds which are not to apply on the capital investment and (*f*) for such part of the net gain as is to be withdrawn as salary or otherwise.

71*g*. The balances shown by the proprietor's or partner's personal or capital accounts are not to be included with accounts receivable or accounts payable, which include only those with outside parties. (¶49 and ¶50)

72. The difference shows the balance owed to or by the proprietor or partner, the same as any other personal account, and the account is closed in the same manner. When the account is to be closed into the proprietor's or partner's capital account, it must be done by a separate journal entry. (¶72*a*).

72*a*. The final disposition of a balance shown by a proprietor's personal account *is determined entirely by the wishes of the individual or by agreement between partners*. When such an account is not credited with any stated salary and is charged with sums withdrawn from time to time, it is not unusual for the account to be closed by debiting the capital account and crediting the personal account for the amount necessary to balance the personal account, which must be done by separate journal entry; or should the personal account show a credit balance which it is desired to add to the capital investment, the personal account may be debited and the capital account credited for the amount to close.

72*b*. Transactions Illustrating the Various Applications of the Rule for Debiting and Crediting the Proprietor's and Partner's Personal Accounts.

Personal account of F. A. Raymond.

The following sums were paid by Mr. Raymond for his personal account: – – Jan. 5. He paid his gas bill, $7.50. (¶71*b*.) – – Jan. 10. He paid his life insurance premium, $47.52 – – Jan. 16. He paid his grocery bill, $31.40. – – Jan. 21. He withdrew cash, $75. (¶71*a*.) – Jan. 25. He paid his house rent, $35. – – Jan. 31. He paid his electric light bill, $3.58.

72*c*. Prepare a ledger account for the above transactions, as instructed in ¶63*a*.

ILLUSTRATION 11.

F. A. Raymond, Personal

19					19			
Jan.	5	Gas bill	C	7 50	Jan.	31	Capital a/c, J	200
	10	Life Ins. premium	C	47 52				
	16	Grocery bill	C	31 40				
	21	Cash	C	75				
	25	House rent	C	35				
	31	Elec. light bill	C	3 58				
				200				200

72*d*. The illustration (11) shows the account as it appears closed at the end of the month, after the journal entry transferring the total amount, $200, to his capital account, had been made and posted as per his instructions. (¶72*a*) The proper journal entry for making the transfer is shown in illustration 12.

ILLUSTRATION 12.

31			
F. A. Raymond Capital a/c		200	
F. A. Raymond Personal a/c			200

EXERCISES IN PROPRIETOR'S AND PARTNER'S PERSONAL ACCOUNTS.

72*e*. Prepare ledger accounts for the following examples:

(1) F. A. Raymond's personal account was debited and credited for the following items during the month of February:

FEB. 3. He collected a bill from a customer and retained it for his private use, $15. (¶71*c*.) – – FEB. 7. A bill for coal used in his residence was paid in cash, $10.50. (¶71*b*) – – FEB. 15. He withdrew cash for his personal use, $100. – – FEB. 18. He paid bill of his family physician, by check, $24. – – FEB. 28. He instructed that his account be credited with his monthly salary of $200. (¶71*f*.) What was the balance shown by his account?

(2) The personal account of B. M. Beck, partner in the firm of Beck & Baldwin, was debited and credited for the following transactions:

APRIL 10. He withdrew cash, on account of salary, $25. – – APRIL 18. He deposited cash in the firm's bank account, $100. (¶71*d*.) – – APRIL 24. He collected from a customer and kept for his personal use, $16 – – APRIL 25. He withdrew, by check, the cash deposited in the firm's account April 18, $100. – – APRIL

30. His account was credited for one month's salary, $150. What was the balance shown by his account?

NOTES RECEIVABLE AND NOTES PAYABLE

73. Notes receivable are the "written promises to pay" of others which are *received* by us.

74. Notes payable are our own "written promises to pay" *given* (issued) to others.

75. Written promises to pay are usually in the form of promissory notes or accepted drafts. (¶15)

ILLUSTRATION 13 A PROMISSORY NOTE

No. 964 Buffalo, N.Y., September 24, 19

Sixty days after date I promise to pay to the order of Gordon, Southard & Co. $743.68

Seven Hundred Forty-three and 68/100 Dollars

payable at Fidelity National Bank

Value received.

Due Nov 23, 19 William B. Allison

ILLUSTRATION 14 AN ACCEPTED DRAFT—ACCEPTANCE

HUNTLEY CREAMERIES

Cornell Brothers, No. 714

Sweetened or Plain Condensed Milk and Cream. Butter & Cheese

Elgin, Ill. June 10 190

Thirty days after sight Pay to the order of Frank B. Cunningham $444.50

Four Hundred Forty-four 50/100 Dollars WITH EXCHANGE

Value received and charge to account of

To Winters, Van Fleet & Co. Boston, Mass.

Cornell Brothers, Inc.

76. They both show a condition of indebtedness, notes receivable corresponding with accounts receivable (¶49) and notes payable corresponding with accounts payable (¶50). The principal difference between a note receivable or a note payable and a personal account is that the one is a *written* promise to pay, and the other is an *oral* or *implied* promise to pay. (¶14)

77. Notes and acceptances are generally received and issued in settlement of personal accounts, thus changing an oral promise to a written promise, which is in fact a written contract.

77a. If A owes B on account and afterwards A gives B his note or acceptance in settlement, while the record of A's indebtedness in B's books is transferred from A's personal account to the notes receivable account, A's indebtedness to B remains just the same, except that in some states and under some circumstances the written promise (note or acceptance) may be more binding upon A.

78. The principal advantage of notes and acceptances is that they are *negotiable*, that is, they are transferable from one person to another, which lends to them the characteristics of *mediums of exchange*, and greatly increases their usefulness in the transaction of business.

79. Because of their negotiability, notes and acceptances are frequently bought and sold, are discounted at bank to raise funds, are transferred "on account," and are sometimes given as security for loans or for debts.

NOTES RECEIVABLE ACCOUNT.

80. Notes receivable account is one of the class in which items relating to *mediums of exchange* are recorded. (¶21, ¶23, ¶78)

81. Notes receivable consist of notes and accepted drafts (acceptances) the value of which we are to *receive* when due.

82. The object of the account is to show (*a*) the amount of notes and acceptances *received* from others, (*b*) the amount of these notes and acceptances which have been redeemed and returned (given back) to those who issued them, or which have been disposed of to others, and (*c*) the amount of notes and acceptances *on hand*, at any date, which is a *resource*.

82a. "On hand" includes all notes and acceptances sent to banks for collection, or in attorney's hands for collection. All notes receivable are considered "on hand" until actual payment has been received. Any note receivable that cannot be collected is a loss.

83. All items must *first* appear on the debit side of this account before they can appear on the credit side, because others' obligations to pay must be received before they can be given back to those who issued them.

Rule for Debiting and Crediting Notes Receivable Account.

84. *Debit what is received: credit what is given.*

84*a*. Debit **notes receivable** (at face value) for notes and acceptances of others *received.*

84*b*. Credit **notes receivable** (at face value) for notes and acceptances of others *given.*

85. The various applications of the rule for debiting and crediting notes receivable are as follows:

86. Debit notes receivable account (*at face value*),—

a. For all notes and acceptances of others invested in the business.
b. For all notes and acceptances received which are made or drawn in our favor.
c. For all notes and acceptances made payable to others and transferred to us by endorsement or otherwise.
d. For all time drafts drawn by ourselves in our own favor, when received after acceptance.

87. Credit notes receivable account (*at face value*),—

e. For all notes and acceptances we hold against others when paid and returned (given back) to them.
f. For all notes and acceptances of others which we sell or have discounted.
g. For all notes and acceptances which we transfer to others "on account" or for any purpose, by endorsement or otherwise.
h. For all part payments received on others' notes and acceptances.

88. **Observe** that in every instance notes receivable account is debited for the amount of notes and acceptances of others *received;* hence the rule.

89. **Observe** that in every instance notes receivable account is credited for the amount of notes and acceptances of others *given* (paid, redeemed, or disposed of); hence the rule.

90. Transactions Illustrating the Various Applications of the Rule (¶84) for Debiting and Crediting Notes Receivable Account.

Jan. 1. Arthur Gordon's note, due on Jan. 15, was invested in the business, $500. (¶86*a*) – – Jan. 4. Received Richardson & Co's note, at 20 days, for $450 (¶86*b*.) – – Jan. 6. Received Moore & Nevin's acceptance in our favor, at 15 days, on account, $375. (¶86*b*.) – – Jan. 15. R. S. Wiley has transferred to us by endorsement, to apply on account, Dane & Ritchie's note, due Feb. 15, for $220.10 (¶86*c*) – – Jan. 15. Received cash in payment of Arthur Gordon's note invested Jan. 1, $500. (¶87*e*.) – – Jan. 17. Received our draft on F. B. Moore, drawn in our own favor at 30 days' sight, for $360.75, which he has returned to us after acceptance (¶86*d*.) – – Jan. 19. Received R. N. Willis' note at 60 days on account, $900. – – Jan. 21. Received cash payment of Moore & Nevin's acceptance of Jan. 6, due today, $375. (¶87*e*) – – Jan. 23. Received King Mfg. Co's acceptance at 60 days, on account, $102.14. – – Jan. 24. Received cash in payment of Richardson & Co.'s note received Jan. 4, due today, $450. – – Jan. 25. Transferred to M. F. Marshall, F. B. Moore's acceptance in our favor, received Jan. 17, on account, $360.75. (¶87*g*) – – Jan. 26. We had R. N. Willis'

note for $900, received Jan. 19, discounted at bank, receiving credit for the proceeds. (¶87*f*) – – JAN. 30. Received Arthur Gordon's note at 60 days, on account, $377.76. – – JAN. 31. Received Moore & Nevin's acceptance at 30 days, on account, $400. – – JAN. 31. Received from King Mfg. Company, in part payment of their acceptance received Jan. 23, $200. (¶87*h*)

What is the balance shown by the account January 31?

EXERCISES.

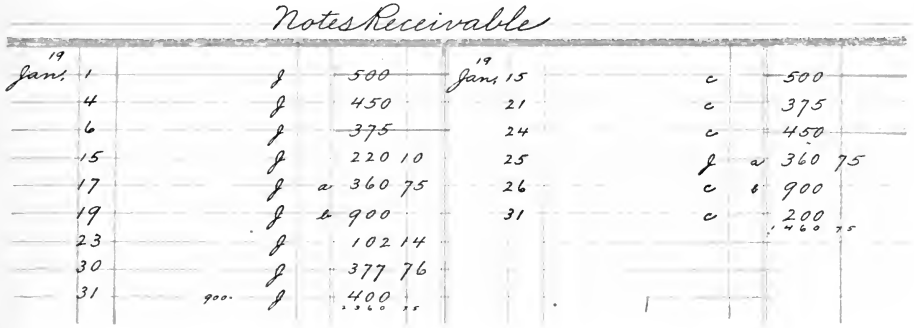
90*a*. Prepare a ledger account for the above transactions on ledger paper, as follows:

(**1**) Read and study each transaction carefully.

(**2**) Read the special application, for each transaction, of the rule for debiting and crediting notes receivable account indicated by the paragraph number.

(**3**) Apply the rule (¶84) and make the proper debit and credit entries in the account, as shown in illustration 15 and submit for approval.

ILLUSTRATION 15.



90*b*. The illustration shows the account as it appears on Jan. 31, with the figures in the posting columns omitted. The small pencil figures show the footings of each column and the balance of the account. (¶40*b*) The letters "aa," "bb," show canceling items. (¶40*c* ¶97)

To Close Notes Receivable Account.

91. The difference between the two sides of the notes receivable account (if any) will show the amount (balance) of others' paper on hand, which is a *resource* that should be included as an item in the statement of resources and liabilities. The sum of the notes and acceptances on hand must agree with the balance shown by account. (¶82*c*)

92. To close. Notes receivable account should never be closed unless the account balances, except when it is necessary to forward the account to another

page when the balance should be entered on the credit side in red ink and forwarded to another page in black ink on the opposite side of the page. (¶98)

93. When all items balance above a given point they may be "ruled out," as shown in illustration 15. It is generally the practice to rule out all items that balance above any two given points on each side of the account, whether they are on the same line or not.

94. When the amounts of the paper received are entered *separately* on the debit side of the account, it is not an uncommon custom to credit the paper, when paid, on the same line on the opposite side of the account. This method, however, frequently disarranges the account, as the credit items may not appear in their chronological order, thereby making the account more difficult to audit.

95. When the amount of each paper is entered separately and the debit side of the account becomes full, many bookkeepers prefer to enter the new debit items on another page, leaving the old account open until all the debit items in that account are credited, the account, consequently, balancing up to that point, rather than to foot and rule the account and forward the balance. This method has the objections referred to in the preceding paragraph.

96. When there are part payments received on the same note or acceptance two or more entries may be made on the same line.

97. Another plan is to check the canceling items on both sides of the account as the entries are made on the credit side, as shown in illustration 15, using the letters of the alphabet to indicate corresponding items. The *unchecked* items on the debit side will then show the different papers on hand and unpaid. This plan is excellent and is highly recommended.

98. When a notes receivable book is kept and used as a posting medium, which is the best practice under all circumstances, only the total amount of the notes and acceptances received during the month appears on the debit side of the ledger account, as shown in illustration 16. If a special column for "Notes Receivable Cr.," is kept in the cash book, only the total of the payments received on notes and acceptance will usually appear in the ledger account, as shown in the illustration; otherwise, a separate credit entry is required for each note or acceptance paid. When a notes receivable book is kept, the suggestions contained in ¶94, ¶95. ¶96 and ¶97 do not apply.

ILLUSTRATION 16.

Notes Receivable

19					19		
Jan. 31		N	3685.75		Jan. 31	C	2785.75
Feby. 28		N	1721.14		Feby. 28	C	791.64
Mar. 31		N	3140.50		Mar. 31	C	1123.93
Apr. 30	2264.62	N	947.31		Apr. 30	C	2528.76
					30 Balance	p	2264.62
			9494.70				9494.70

98*a*. This account corresponds with accounts receivable account (¶49, ¶54*a*) except that it shows others' *written* promises to pay instead of oral promises to pay. The balances in both accounts show *resources*. The amounts on the debit side show the total notes and acceptances received for the month. "N" indicates that they were posted from the note book. The credit items show the total receipts of cash in payment of notes and acceptances receivable for the month. "C" indicates the cash book, and as there is only one credit item for the month, it indicates that a special column with "Notes Receivable Cr." is kept in that book. The account is shown balanced and ruled, ready to be forwarded. Illustration 17 shows the account opened on another page with the balance transferred.

ILLUSTRATION 17.

Notes Receivable

19			
May 1	Balance	p	2264.62

EXERCISES IN NOTES RECEIVABLE ACCOUNTS.

99. Prepare the ledger accounts for the following examples, applying the rule (¶84) in each transaction. Rule out the items that balance on each side of the account as the balancing credit entries are made. Follow the special instructions for each example carefully.

(**1**) The transactions in George Warren's books relating to notes receivable are as follows:

FEB. 1. He invests in the business William Brown's 30-day note, dated Jan. 15, for $250.16; also James Dean's 60-day acceptance, dated Jan. 13, for $311.17. – – FEB. 5. He receives from R. M. Walters his note at 30 days, dated February 2, for $364; also H. A. Harvey's acceptance at 30 days, dated January 28, for $276.50. – – FEB. 10. J. Watkins & Co. transfers to him C. N. Laws' acceptance at 30 days, dated Feb. 2, for $300, to apply on account. – – FEB. 14. He receives payment for William Brown's note of Jan. 15, $250.16. (*Rule out balancing items.*) – – FEB. 15. He transfers H. A. Harvey's acceptance of Jan. 28 at 30 days to A. C. Hatfield, to apply on account, $276.50. – – FEB. 18. He had James Dean's acceptance of Jan. 13 discounted at bank, $311.17. – – FEB. 25. R. W. Day accepted and returned his draft at 30 days after date for $116.40.

What is the balance of his notes receivable account February 28? Indicate canceling items by using the letters alphabetically, beginning with the first credit item.

(2) Louis Bessler & Co's notes receivable account contains entries for the following transactions:

JULY 1. They invested four notes made by Rand & Co., all dated June 15,—one at 30 days for $200, one at 40 days for $300, one at 50 days for $400, and one at 60 days for $376.18. – – JULY 6. They received from James Ross, on account, his acceptance at 30 days for $275. – – JULY 10. They received in payment for merchandise sold to Bennett & Sons their note at 30 days for $275. – – JULY 12. Charles Adams transferred to them J. Harman & Co.'s note, dated July 1, at 30 days, to apply on account, $125. – – JULY 15. They received cash from Rand & Co., in payment of note of June 15 at 30 days, $200. (*Rule out balancing items.*) – – JULY 18. They transferred Rand & Co.'s note of June 15 at 40 days to First National Bank for collection. (No entry is made until the collection is reported by the bank. (Read 82*a*.) – – JULY 20. They transferred James Ross' acceptance of July 6 to Hatfield Bros., to apply on account, $275. – – JULY 25. The First National Bank notified them that they have collected Rand & Co.'s note left for collection July 18, and have placed the amount to their credit, $300 – – JULY 30. They had Rand & Co.'s note at 60 days discounted at bank, $376.18. – – JULY 31. They received in part payment of J. Harman & Co.'s note of July 1 at 30 days $75.

Indicate canceling items as previously instructed.

(3) JAN. 1. Redmond Bros. received note of Arthur Jones, dated Dec. 20 at 30 days, for $650; also J. M. Pugh's note, dated Dec. 8 at 60 days, for $700. – – JAN. 5. They received Jones & Jones' note, dated Jan. 1 at 30 days, for $250; they also received Adams Bros. acceptance, dated Dec. 24 at 30 days, for $236.75. – – JAN. 10. W. A. Andrews transferred to them H. A. Kelly & Co.'s acceptance, dated Jan. 2 at 30 days, for $350, to apply on account. – – JAN. 19. They received cash in payment of Arthur Jones' note of Dec. 20 for $650. (*Rule out balancing items on the same line.*) – – JAN. 20. They had J. M. Pugh's note of Dec. 8 discounted at bank, receiving credit for the proceeds, $700. (*Rule out balancing items.*) – – JAN. 25. They transferred Jones & Jones' note of Jan. 1 for $250 to R. M. Wade & Co. on account. (*Rule out balancing items.*) JAN. 30. Received cash of H. A. Kelly in payment of his acceptance, $350.

What is the balance shown by their notes receivable account Jan. 31?

Indicate canceling items as heretofore instructed.

(4) Transactions relating to notes receivable in the books of Davis & Co. JULY 3. Received R. B. Small's note, dated July 1 at 30 days, on account, $500; also Duncan & Kane's note, dated June 8 at 30 days, $450. – – July 5. Received from W. H. Corwin on account his note dated July 2 at 2 months, $159.38. – – JULY 6. Received from D. A. Davidson, to balance account, his note dated July 3 at 30 days, $237.45. – – JULY 6. R. B. Small prepaid his note in cash, $500. (Rule) – – JULY 7. Received from J. A. Gilman our draft of July 3,

on him at 30 days' sight, which he returns accepted July 6, $376.50. – – JULY 8. Received Duncan & Kane's check in payment of their note, due today, $450. – – JULY 9. Received from A. B. Jones his note at 30 days, in full of account, $300. – – JULY 11. Sold G. A. Mann & Co., for their note at 30 days, merchandise, $574.50. – – JULY 15. Received from E. Norton his draft in our favor at 30 days' sight, on W. W. Colburn, which was accepted July 15, $458.47. – JULY 18. Received from F. R. Perkins his note at 30 days, on which we loaned him cash, $400.

(5) Adam Ross, conducting an installment business, receives the following notes: AUG. 2, note from A for $100, dated Aug. 1, payable $10 per month; note from B for $50, dated Aug. 1, payable $5 per month; note from C for $60, dated Aug. 1, payable $6 per month. – – SEPT. 1. A, B, & C pay their installments. OCT. 1. A & C pay their installments. – – Nov. 1. He received note from D for $36, payable $4 per month. – – Nov. 2. B & C pay all installments to date. – – DEC. 1. A, B, C & D pay all installments due to date.

Use letters of alphabet to denote payments applying against their respective notes. What is the balance shown by the account?

When these accounts have been carefully prepared, submit them for approval.

NOTES PAYABLE ACCOUNT.

100. Notes payable account is one of the class in which items relating to *mediums of exchange* are recorded. (¶21*b*, ¶23, ¶78)

101. Notes payable consist of our own notes and of accepted drafts (acceptances) the value of which we are obligated to *pay* when due. (¶77)

102. The object of this account is to show (*a*) the amount of our notes and acceptances issued to others, (*b*) the amount of these notes and acceptances which have been redeemed by and returned to us, and (*c*) the amount we still owe on outstanding notes and acceptances at any date, which is a *liability*.

103. Bonds or mortgages payable should not be included in the ordinary notes payable account, but should be kept in separate accounts, under appropriate titles. Likewise bonds and mortgages receivable should be kept in separate accounts. Not infrequently the account for such securities is kept under the title "Bonds and Mortgages Receivable," or "Bonds and Mortgages Payable."

104. All items that appear on the debit side of this account must *first* appear on the credit side, because our obligations to pay must be issued before they can be redeemed.

Rule for Debiting and Crediting Notes Payable Account.

105. *Debit what is received: credit what is given.*

105*a*. Debit **notes payable** (at face value)—for our notes and acceptances *received* (paid and redeemed).

105*b*. Credit **notes payable** (at face value)—for our notes and acceptances *given* (issued).

106. The various applications of the rule for debiting and crediting notes payable are as follows.

107. Debit notes payable account (at face value),—

a. For all our notes and acceptances when paid or redeemed and received back by us.

b. For all part payments made on note and acceptances issued by us.

108. Credit notes payable account (at face value,—

c. For all notes and acceptances held by others against us at the beginning of business.

d. For all our notes given (issued) and for all drafts accepted by us in favor of others.

109. **Observe** that in every instance notes payable account is debited for the amount of our own notes and acceptances when paid, redeemed and *received back* by us; hence the rule.

110. **Observe** that in every instance notes payable account is credited for the amount of our own notes and acceptances issued or *given out* to others by us; hence the rule.

111. Transactions Illustrating the Various Applications of the Rule for Debiting and Crediting Notes Payable Account.

Jan. 1. F. A. Raymond owed on his note, in favor of R. S. Walters & Co., due Jan. 16, $200. (¶108*c*) – – Jan. 4. He gave his note at 20 days to Peterson & Co., on account, $633.45. (¶108*d*) – – Jan. 9. He accepted Rich & Hartley's draft at 10 days' sight for $89.73 in full of account. (¶108*d*) – – Jan. 16. He gave his note to Alex. Chester Sons at 30 days in full of account, $1,137.68. – – Jan. 19. He paid his acceptance of Jan. 9 in cash, $89.73. (¶107*a*) – – Jan. 21. He accepted Brown Bros. draft, in their own favor, at 10 days, in full of account, $113.39. – – Jan. 24. He gave Bennett & Sons his note at 30 days on account, $150. On the same date he paid his note, issued Jan. 4, due today, $633.45. – – Jan. 26. He paid his note, due today, in cash, $200. (*Rule out balancing items.*) (¶116) – – Jan. 30. He accepted J. H. Van. Sickle's draft at 30 days, in full of account, $212.32. – – Jan. 31. He paid acceptance of Jan. 21, $113.39.

What is the balance shown by the account Jan. 31?

111*a*. Prepare a ledger account for the above transactions, as instructed in 90a, applying the rule (¶105) in determining the proper entries. Indicate canceling items. Prove the account by seeing that the sum of the unchecked items equals the balance, and submit for approval.

ILLUSTRATION 18.

Notes Payable

19				19			
Jan.	19	c	89 73	Jan.	1	J	200
	24	c	633 45		4	J	633 45
	26	c	200		9	J	89 73
	31	c	a 113 39		16	J	1137 68
					21	J	a 113 39
					24	J	150
					30	1500 J	212 32
							1613 39

111*b*. The illustration shows the account as it appears Jan. 31, with the figures in the posting columns omitted. The small figures showing the footings and the balance of the account are *pencil* figures which are inserted when the trial balance is taken. (¶40*b*). Notice that the first three items on each side of the account are canceling items and are ruled out (¶114) after the third entry on the debit side of the account is made. They could also be indicated by letter, as is illustrated for the canceling items marked "*a, a.*" The sum of the uncanceled items should equal the balance of the account. (¶115).

112. The difference between the two sides of the notes payable account (if any) will show the amount of our notes and acceptances outstanding, which is a *liability* that should be included in the statement of resources and liabilities (see 93). All items must first appear on the *credit* side of the account. The sum of the notes and acceptances outstanding must equal the balance shown by the account.

113. To close. Notes payable account should never be closed unless the account balances, except when it is necessary to forward the account to another page, when the balance should be entered in red ink and forwarded in black ink on the *opposite* side of the page. (¶116*a*)

114. When all items balance above a given point they may be "ruled out," as shown in illustration 18. (¶111*b*) It is the general practice to rule out all items that balance above any two given points on each side of the account, whether they are on the same line or not.

115. When the amounts of paper issued are entered *separately* on the credit side of the account, each item, when paid, may be debited on the same line on the opposite side of the account. This method has objectionable features. (¶94) When the credit side of the account becomes full it is generally preferable to open the new account as suggested for notes receivable. (¶95) When part payments are made on the same note or acceptance, two or more entries may be made on the same line. As the entries showing full payment are made on the debit side, the amounts may be canceled on both sides of the account. (See *a, a*) The uncanceled items on the credit side show the different papers outstanding and unpaid. (¶111*a*)

116. When a notes payable book is kept and used as a posting medium, which is the best practice, only the total amount of the notes and acceptances issued for the month will appear in the ledger account, as shown in illustration 19. When a special column for "Notes Payable Dr." is kept in the cash book, only the total amount of our notes and acceptances redeemed for the month will usually be shown in the ledger account; otherwise the amount of each note or acceptance paid will appear separately on the debit side of the account.

ILLUSTRATION 19.

Notes Payable

19				19			
Jan. 31		c	1036 57	Jan. 31		n	2536 57
Feby. 28		c	1643 62	Feby. 28		n	548 96
Mar. 31		c	893 65	Mar. 31	754.13	n	1242 44
	31 Balance	fr.	754 13				
			4327 97				4327 97

116*a*. Notes payable account corresponds with accounts payable account (¶50) except that it shows our *written* promises to pay instead of oral promises to pay. The balances in both accounts show *liabilities*. The illustration above shows the account as it appears when the notes payable book is used as a posting medium and a special column for "Notes Payable Dr." is kept in the cash book. On the opposite page the account is shown with the balance transferred. (¶113).

ILLUSTRATION 20.

Notes Payable

19			
Apr. 1	Balance	fr.	754 13

EXERCISES IN NOTES PAYABLE ACCOUNTS.

117. Prepare the ledger accounts for the following examples, applying the rule (¶105) in each transaction. Rule out the items that balance on each side of the account as the balancing debit entries are made. Follow carefully the special instructions for indicating the canceling items.

(1) The transactions in Brown Bros. & Co.'s books relating to notes payable are as follows:

JAN. 1. Gave J. Doris note at 10 days, on account, $280. – – JAN. 6. Accepted Charles Paxton's draft dated Dec. 30 at 30 days after date, for $316.40 – – JAN. 11. Paid note in favor of J. Doris, $280. (*Rule*) – – JAN. 12. Gave Jas. Davis our note at 30 days for $328 in full of account. – – JAN. 19. Made part payment on our acceptance of Jan. 6, $200. (¶107*b*) – – JAN. 21. Gave E. N. Ray, note at 30 days, in full of account, $276.14. – – JAN. 22. Paid balance due on our acceptance of Jan. 6, $116.40.

Indicate canceling items (¶111*b*) and show the balance of the account, Jan. 31.

(2) MARCH 1. Frank Brown began business, owing the following notes:

Note in favor of John Bentz, dated Feb. 16 at 30 days for $847.19; note in favor of Gard Mfg. Co., dated Feb. 25 at 60 days, $540.16; note in favor of the City National Bank, dated Feb. 15, payable on demand, for $2,000. – – MARCH 5. He gave his note at 30 days to Gard Mfg. Co. for $350.75. – – MARCH 6. He accepted Knight & Day's draft at 30 days' sight for $219.54. – – MARCH 9. He accepted Maxwell & Co.'s draft at 60 days, for $685.20. – – MARCH 10. He made part payment on note held by City National Bank, $500. – – MARCH 18. He took up note in favor of John Bentz, dated Feb. 16, by giving him cash $500, and a new note at 30 days for $347.19 (*Debit the account for the old note; credit it for the new note.*) – – MARCH 18. He made part payment on note held by the City National Bank, $500. – – MARCH 25. He sold merchandise to Gard Mfg. Co., who transferred back to him his note of March 5 at 30 days for $350.75, in part payment. (¶107*a*) – – MARCH 30. He paid note in full held by City National Bank, $1,000.

Indicate canceling items by letter. (¶115)

(3) JAN. 1. Robinson & Kennedy enter into a partnership, bringing into it all the resources and liabilities of their former separate businesses. Robinson owed a note, dated Dec. 15 at 30 days in favor of A. C. Boyd, for $275. (¶108*c*) Kennedy owed a note dated Dec. 20 at 60 days in favor of J. M. Byrnes for $300; also his acceptance of Dec. 10 at 30 days in favor of Boyd & Johnson for $116.42. – – JAN. 5. They borrowed from the Merchants National Bank on their note payable on demand, $5,000. – – JAN. 8. They issued their note at 40 days to Andrews & Co., for merchandise, $257.10 – – JAN. 10. They accepted Jones & Co's draft at 10 days' sight for $278.19. – – JAN. 10. They paid their acceptance in favor of Boyd & Johnson, $116.42. – – JAN. 14. They paid their note in favor of A C. Boyd, dated Dec. 15, for $275. – – JAN. 15. They paid the Merchants National Bank $500, to apply on their note issued Jan. 5. – – JAN. 20. J. M. Byrnes transferred to them Kennedy's note of Dec. 20, for $300, in part payment of goods sold him that day. – – JAN. 26. They accepted W. N. Davidson's draft at 30 days for $398. – – JAN. 28. They made a payment on the note issued Jan. 5 in favor of the Merchants National Bank, $1,000. – – JAN. 30. They took up their demand note issued Jan. 5 in favor of the Merchants National Bank, by paying the balance in cash.

Indicate canceling items by letter, beginning with the first debit item. To find the balance due on note in favor of the Merchants National Bank, indicate the payments on Jan. 15 and Jan. 28, "*d, d.*" Where the entry for the full payment of the note is made on Jan. 31, indicate that item and the credit entry of Jan. 5 with the same letter. By this method the account will show the three items on the debit side that cancel the one item on the credit side of the account. Show the balance of the account on Jan. 31.

(4) John Adams had notes and acceptances outstanding at the beginning of business, June 1, as follows:

JUNE 1. A note dated May 10 at 30 days in favor of Anson Byrd & Co., for $200; a note dated May 20 at 40 days in favor of Anson Byrd & Co., for $165.40; an acceptance dated May 15 at 60 days in favor of Calhoun & Co., $316.20; and an acceptance dated May 27 at 15 days in favor of Wells & Wright, for $95.40. These were all issued in payment of bills purchased to begin business. The following transactions occurred during the month:

JUNE 5. Accepted Vermont Stone Co's draft at 30 days' sight, $187.60. – – JUNE 9. Took up note of May 10 in favor of Anson Byrd & Co., for $200, by paying $100 in cash and issuing a new note at 10 days for $100. – – JUNE 11. Paid acceptance in favor of Wells & Wright, due today, $95.40. – – JUNE 19. Paid note issued June 9, for $100. – – JUNE 29. Paid note of May 20 in favor of Anson Byrd & Co., $165.40. – – JUNE 30. The Vermont Stone Co. returned acceptance of June 5 in part payment of goods purchased.

Follow previous instructions.

(5) AUG. 1. On commencing business, John Thompson owed an acceptance due Aug. 16 in favor of J. L. Soule, for $525. – – AUG. 2. He issued note at 30 days to G. H. Mann, for $350. – – AUG. 15. He accepted E. H. Davis' draft at 30 days' sight in favor of H. K. Moore, for $196.34. – – AUG.16. He paid acceptance in favor of J. L. Soule. – – AUG. 17. He accepted M. M. Brown's draft at 10 days' sight in favor of J. V. Chase, for $257.43. – – AUG. 27. He paid his acceptance due that day. – – AUG. 28. He received from W. J. Tucker, on account, his note issued Aug. 2 to G. H. Mann.

What was the balance shown by his notes payable account, Aug. 31?

On Sept. 3, Mr. Thompson accepted a draft at 10 days' sight $150. He paid this and his acceptance of Aug. 15 at maturity. Make the proper entries under the proper dates, and show the account closed and ruled as it would appear Sept. 30. (¶113).

CASH ACCOUNT.

118. Cash includes gold, silver, and coins, bank notes, U. S. Treasury notes, money orders, bank drafts, checks, and whatever else is received or given as money. Cash is the most important of the *mediums of exchange.* (¶21)

119. The object of this account is to show the *receipts* and *payments* of cash, and from these to ascertain the *amount of cash that should be on hand.* (¶23)

119*a*. "On hand" includes the cash in the safe or drawer, to which must be added the balance in bank shown by the check book, or by the "check and deposit book." When accounts are kept in more than one bank, the sum of the balances must be added to the cash in safe or drawer. When a separate ledger account is kept with the bank, "cash on hand" includes only the actual cash in the safe or drawer. Ledger accounts with banks are seldom kept.

120. The cash account is seldom kept in the ledger but is kept in a separate cash book in which the entries for all receipts and payments of cash are made and from which they are posted to the proper accounts in the ledger. When the cash book is kept, no cash items are entered in any other book.

Rule for Debiting and Crediting Cash Account.

121. *Debit what is received: credit what is given.*

121*a*. Debit **cash** when *received.* (Debit for *receipts.*)

122*b*. Credit **cash** when *given.* (Credit for *payments.*)

122. The various applications of the rule are few, and are as follows:

123. Debit cash account,—

a. For the amount of cash invested in the business.

b. For all cash received thereafter.

124. Credit cash account,—

c. For all cash paid out.

d. For all cash loaned to others or lost.

e. For all checks issued (when no bank account is kept in the ledger).

f. When a bank account is kept, for all cash deposited.

125. Observe that in every instance the account is debited for the amount of cash received (receipts).

126. Observe that in every instance the account is credited for the amount of cash given (payments).

ILLUSTRATION 21.

Cash Receipts

19								
Jan.	1	F. A. Raymond Cap. a/c.	Investment	5000				
	5	R. J. Maclean & Co.	On a/c.	100				
	8	H. B. Wilson	Bill of Jan. 2 1	361	02			
	9	Jamison & Fox	On bill of Jan. 4	75				
	11	Notes Receivable	Dennis Bros. note	212	50			
	11	Interest	60 ds. on D. B. note	2	13			
	12	Sales	Cash sales	17	65			
	14	Archer & Lane	Bill Jan. 8	427	38			
	19	White & Gates Co.	In full of acct.	19	31			
	21	Jamison & Fox	In full bill Jan. 4	67	94			
	25	Notes Receivable	Archer & Co's note	114	22			
	27	A. M. Peters	On a/c.	200				
	30	Notes Payable	Borrowed on note at 30 ds.	500			7097	15
							7097	15
Feby.	1	Balance		2444	21			

127. TRANSACTIONS ILLUSTRATING THE VARIOUS APPLICATIONS OF THE RULE (¶12) FOR DEBITING AND CREDITING CASH ACCOUNT.

F. A. Raymond's cash transactions are as follows:

JAN. 1. He invested cash, $5,000. (¶123*a*) – – JAN. 3. He paid Sharp & Co.'s coal bill, $16. (¶124*c*) – – JAN. 4. He paid John Ward for bill of Dec. 26, $496.75. – – JAN. 5. He received cash from R. J. Maclean & Co. on account, $100 (¶123*b*) – – Jan. 6. *He paid cash for blank books and stationery, $21.50 (¶124*c*) – – JAN. 8. He received cash from H. B. Wilson, for billof Jan. 2, $361.02 – – JAN. 9. He received cash from Jamison & Fox, to apply on bill of Jan. 4, $75. – – JAN. 10. He paid freight bill on goods purchased, in cash, $7.66. – – JAN. 11. He received cash in payment of Dennis Bros. note, $212.50; he also received cash in payment of interest on the same, $2.13. – – JAN. 12. He received cash for cashsales of goods, $17.65. On the same day he paid for stamped envelopes $3.20. – – JAN. 14. He received cash of Archer & Lane, for bill of Jan. 8, $427.38. – – JAN. 15. He paid W. J. Brown for his bill of Jan. 4, $987.50. – – JAN. 19. He received cash from White & Gates Co., in full of account, $19.31. – – JAN. 19. He paid his note in favor of Gill & Co., $350, and interest on the same $1.75. – – JAN. 21. He received cash from Jamison & Fox, in full for bill of Jan. 4, $67.94. – – JAN. 25. He received payment of Archer & Co's note, $114.22. – – JAN. 27. He paid cash to Waters & Smith, for bill of Dec. 27, $2,491.48. – – JAN. 27. He received cash from A. M. Peters on account, $200. – – JAN. 30. He paid rent for January, $125. – – JAN. 30. He borrowed on his note at 30 days, $500. – – JAN. 31. He paid salesmen's salaries in cash, $80; warehouse labor, $22.10; and he withdrew for his personal use, $50.

What should be the balance of cash on hand Jan. 31?

*"Ad. Expense" is the abbreviation for administration expense.

Cash Payments

19 Jan.	3	Genl Expense	Shaw & Co. Coal bill	16		
	4	John Ward	Bill of Dec. 26	496	75	
	6	Adv. Expense	Blank books & stationery	21	50	
	10	Purchases	Freight bill	7	66	
	12	Adv. Expense	Stamped envelopes	3	20	
	15	W. J. Brown	Bill of Jan. 4	987	50	
	19	Notes Payable	Note favor Gill & Co.	350		
	19	Interest	On note favor G. & Co.	1	75	
	27	Walters & Smith	Bill of Dec. 27	2491	48	
	30	Genl Expense	Rent for Jan.	125		
	31	Sales Expense	Salesmens salaries	80		
	31	Purchases	Warehouse labor	22	10	
	31	F. A. Raymond & Co.	For personal use	50		4652 94
	31	Balance				2444 21
						7097 15

127*a*. Prepare a cash book account for the above transactions on journal paper, as follows:

(**1**) Read and study each transaction carefully.

(**2**) Read the special application for each transaction of the rule for debiting or crediting cash account, indicated by the paragraph number.

(**3**) Study carefully the information contained in paragraphs ¶128 to ¶128*c* following illustration 21.

(**4**) Apply the rule (¶121) and make the proper debit and credit entries in the cash book, as shown in illustration 21, referring to the illustration to determine the proper accounts to be named in connection with each debit and credit item. When completed, submit for approval.

128. The cash book in addition to the columns for the date, the posting figures, and the amount of each item shown in an ordinary account, contains two additional columns on each side—one for the name of the opposite, or *contra*, account affected, and another for an explanation of the item.

128*a*. All items of cash received and entered on the *debit* (left) side of the cash book are posted to the *credit* side of the ledger account named.

128*b*. All items of cash paid out and entered on the *credit* (right) side of the cash book are posted to the *debit* side of the ledger account named.

128*c*. The cash book may and usually does contain a number of columns that greatly reduce the work of the bookkeeper, facilitate posting, and guard against errors. Their use also assists in the analysis of receipts and payments, which is of great value in an audit. The use of special colums is explained elsewhere in this work.

To Close Cash Account.

129. The difference (if any) between the two sides of the cash account will always show a *debit* balance *which should equal the amount of cash on hand*, which is a *resource* that should be included in the statement of resources and liabilities. The credit side of the account can never be the larger since it is impossible to pay out more cash than is received.

129*a*. The credit side may be made the larger by "overchecking" on the bank, but this is a violation of banking rules, and the account should never be closed showing an overdraft.

129*b*. It sometimes happens that a bank account will show an over-draft caused by checks which are issued to parties residing at a distance and which consequently, will not reach the bank on which they are drawn for payment for a considerable time. In such cases the cash account will show a credit balance.

130. To close. Find the difference. Then enter on the credit side in red ink (1) the amount of the difference, (2) the date and (3) the word "Balance." Then rule and foot the account as shown in illustration 21 and bring down the balance on the *opposite* side (in black ink), entering the date of the next business day.

Exercises in Cash Accounts.

131. Prepare cash book accounts for the following examples, applying the rule (¶121) in each transaction. The words in italics in each transaction indicate the names of the accounts affected (¶128). Be careful to make the explanation complete. After the entries are made, balance, rule and foot each example, and bring the balance down on the opposite side. When completed, present for approval.

1. G. R. Gilman's receipts and payments of cash are as follows:

April 1. *G. R. Gilman* invests $3,000. – – April 3. He paid *H. D. Page*, for bill of March 26, $115.25. – – April 4. He received from *Charles Clark*, on account, $35. – – April 5. He paid coal bill of April 3, $16, which is a *general expense*. – – April 8. He received cash from *H. M. Brown* for bill sold March 6, $76.40. – – April 9. He paid *John M. Ward* in full of account, $36.85. – – April 10. He received from cash *sales*, $22.50. – – April 15. He paid McClellan & Co. for office books and stationery, which is an *administration expense*, $26.70. – – April 21. He received cash in payment of William Gray's note, which affects *notes receivable* account, $314.32. – – April 23. He received from *Reynolds Bros.* for bill sold Feb. 26, $50. – – April 26. He received from *Sharp & Co.* in full of account to date, $36.12. – – April 26. He paid for cleaning the office windows, which is a *general expense*, $1.15. – – April 29. He received from *B. F. Cole* for bill of April 15, $116.45. – – April 30. He received from cash *sales*, $135.35. – – April 30. He paid for stamps, $3; pencils, $2; gas bill, $5; salary of bookkeeper, $50; which are *administration expenses*.

What is the balance of cash which should be on hand or in bank, April 30? If $2,500 has been deposited in bank, how much should be in the cash drawer?

2. The following transactions are taken from the books of H. C. Shepard & Co.

SEPT. 1. *H. C. Shepard* invested $6,000; *M. A. Shepard*, $1,000. – – SEPT 3. *Purchases* for cash were $61.75. – – SEPT. 4. Cash *sales* were $42.85. – – SEPT. 6. Cash *sales* were $36.70. – – SEPT. 7. Paid *Henry Smith*, on account, $200. – – SEPT. 8. Received from *William Wright*, for bill of July 6, $212.35. – – SEPT. 10. Paid for insurance on stock, which is a *general expense*, $48; received from *W. B. Page*, for bill of Sept. 5, $137.25. – – SEPT. 11. Received payment for H. M. Jones' note (*notes receivable*) $200. – – SEPT 11. Paid cash for advertising bill, which is a *sales expense*, $13.50. – – SEPT. 12. Paid cash for bill heads, which is an *administration expense*, $6. – – SEPT. 13. Paid note (*notes payable*) due today at bank, $250. – – SEPT. 16. Received from *James Harris*, cash for bill of August 15, $457.19. – – SEPT. 18. Paid *Henry Wilson* for bills of Sept. 7 and 13, $498.20.

What were the total receipts of cash, the total payments, and the balance on hand? If all cash received was deposited in bank, and all payments made by check what should be the balance of cash in bank?

131*a*. Find the results for the following transactions arithmetically, placing the receipts in one column and the payments in another. It is unnecessary to prepare a cash book form.

1. JAN. 1. Levi Price and John G. Price each invested $2,000. – – 2. Advanced William Brown for traveling expenses, $50. – – 4. Received from William H. Walker for bill of Jan. 3, $353.09. – – 6. Paid C. W. Perkins for bill of Dec. 27, $651.75; also paid for books and stationery, $23.50. – – 8. Received from D. H. Gordon, on account, $250. – – 9. Paid Frank Morrison, on account of bill of Jan. 3, $540. – – 12. Received from John Mitchell, to apply on account, $150. – – 15. Paid rent for Jan. ,$60. – – 17. Received from F. P. Draper, in payment of bills of Dec. 26 and Jan. 3, $343.12. – –18. Paid G. B. Dean & Co., for bill of Jan. 17, $542. – – 19. Received from C. T. Richardson, in full of account to Jan. 12, $197.23. – –25. Levi Price withdrew $60 for personal use, and John G. Price withdrew $100 for personal use. – – 26. Received from Frank Young, in payment of his note, due today, $100. – – 27. Paid John Sater, in full of account, $614.21. – – 31. Cash sales, $161.27. – – 31. Paid for janitor service, $15; coal bill, $7.50; salaries of bookkeeper, $45, stenographer, $36.

What should be the balance of cash on hand January 31? If all sums received were deposited, except cash sales of January 31, and all payments made by check except those of January 31, how much cash should be in the cash drawer and how much in bank?

2. JAN. 1. Joseph Franklin invested $5,000. – – 2. Bought two tons of coal for cash, $13. – – 2. Received from Willis Bros., in payment of bill of Dec. 26, $362.50. – – 3. W. B. Weeks paid his note due today, $300; and interest, $3.00

– – 4. Paid Wells & Ray for their bill of Dec. 27, $259.17. – – 4. Paid for printing letter heads and envelopes, $12. – – 4. Cash sales, $21.36. – – 5. Bought merchandise for cash, $86.15 – – 7. Received from Harry Arnold, payment in full of account, $388.09. – – 9. Bought new desk from Keeler & Co., $45. – – 9. Paid Ratcliffe Co., for boxes, $32.15. – –10. Cash sales, $17.14; also received from A. G. Osgood, in payment of bill of Jan. 3, $185.17. – – 11. Paid incoming freight and express bills, $38.56. – – 12. Bought two horses, wagon and harness, complete, from Adams Bros., for $350. – – 13. Paid for hay $6; straw, $3.50. – – 13. Received from R. A. Walters, in full of account, $218.60; also received payment of Dilworth Bros. note, due today, $468.18; and interest, $7.02. – – 15. Cash sales, $17.05. – – 15. Received from Russell Bros., on account, $100. – – 18. Paid interest on note at bank, $15. – – 18. Paid for repairs on wagon, $4.50. – – 20. Cash sales. $14.85. – – 21. Received from John Richards, on account, $45. – – 22. Paid gas bill, $10.85; also advertising bill, $8.20. – – 25. Received from C. C. Miller, in full of account, $147.18. – – 28. Paid George Cromwell for invoice of Jan. 13, $412.11 – –31. Cash sales, $114.16 – – 31. Paid rent of building, $100; clerk hire, $100; postage, $5; sundry expenses, $3.12.

What should be the balance of cash on hand? If $\frac{1}{3}$ was in the cash drawer and $\frac{2}{3}$ in bank, what was the amount in bank?

MERCHANDISE ACCOUNTS.

132. Merchandise is a general name given to any commodity that is bought for the purpose of selling it at a profit. (¶21*c*, ¶24)

133. As the principal profit of a mercantile or trading business is derived from the buying and selling of merchandise, those accounts in which are recorded the various items entering into the *cost of the goods purchased* and the various items affecting *the returns from the goods sold* are of first importance, as they provide the data from which the *gross profit from sales* is determined. These are known as *trading* accounts. From them the *trading statement* is made up. (¶233) This statement is one of the most important statements made in connection with bookkeeping or accounting. It supplies information that is necessary to an economical and profitable administration of a business.

133*a*. NOTE: A comparison of the results shown by the various accounts relating to the buying and selling of merchandise, from year to year, makes possible an analysis of the business, particularly of the sources of profit and of loss, that is invaluable in building it up and strengthening the weak spots, cutting off an expense here, increasing a profit there. This is a necessity in profitable business management.

PRINCIPAL AND SUBSIDIARY TRADING ACCOUNTS

134. The accounts in which are recorded the items relating to the purchase and sale of goods are divided into two classes—*principal* accounts and *subsidiary* accounts.

135. The principal accounts are the *purchases* account, the *sales* account and the *inventory* account.

136. These three accounts correspond with the three principal operations incidental to conducting a mercantile business, namely: *purchasing* merchandise, *selling* merchandise (which are more or less continuous operations) and the taking of the *inventory* at the time of closing the books, which operation occurs at the close of each fiscal period for which the business is conducted, generally once a year; therefore, the purchases and the sales accounts are continuing accounts, while the inventory account receives entries only at the closing of the ledger for the fiscal period.

137. There are a number of different items such as freight, express and drayage charges, allowances and rebates, and other items, varying in different lines of business, which relate to the purchases and sales accounts, and contribute to increasing and diminishing both the cost of purchases and the returns (proceeds) from sales. Several of these items are usually entered directly into the purchases and sales accounts (¶151, ¶152, ¶153, ¶164, ¶165, ¶166) while others are entered in special, or subsidiary, accounts which are fully explained under the proper heading. (¶176)

138. *The subdivision* of the accounts relating to the purchase and sale of merchandise into the principle and subsidiary accounts illustrates an important principle of accountancy, which is that *each account should show but one specific thing or result*; and it follows, therefore, that a separate account should be opened and kept for each particular item of information which it is desired that the books should show or that should appear in the trading statement.

139. *This method* has an important educational advantage because it permits the *one particular purpose* of an account to be fully explained so that it may be clearly understood by the student. It has an equally important *practical* advantage in supplying the data to make intelligent comparisons between the results shown by the various accounts for different fiscal periods.

PURCHASES ACCOUNT—A PRINCIPAL TRADING ACCOUNT

140. The object of the purchases account is to show the *cost of purchases* for the fiscal period covered in the account. "Purchases" includes only those goods bought to be sold. The *debit* side of the account shows the cost of goods purchased, (gross purchases) from which is deducted the value of any goods returned, of rebates, allowances, and of other items that have the effect of *decreasing the cost of purchases*, these items appearing on the *credit* or *contra* side of the account.

141. The cost of purchases in wholesale and jobbing businesses includes not only the invoice price of the goods, but also the cost of any freight, express, drayage or other charges on the goods, of commissions for buying, and of all other expenses

necessary *until the goods are ready for delivery to the local customer, or are on board cars for shipment.* In retail businesses, department stores, etc., *when the goods are ready for sale* (i. e. are placed on the shelves or in show cases in stockroom) *the costs end* and the *selling expenses begin.*

Rule for Debiting and Crediting Purchases Accounts.

142. *Debit for costs: credit for returns.*

142*a*. Debit **purchases** account for the *costs* of purchases and charges.

142*b*. Credit **purchases** account for goods returned by us, and rebates and allowances to us on purchases.

143. The various applications of the rule are as follows:

144. Debit purchases account,—

a. For all merchandise purchased.

b. For* incoming freight, express and drayage, (¶184) for duties, storage, and for other similar charges.

c. For* purchasing agents' commissions salaries or expenses for buying goods.

d. For boxing, packing and shipping material (*warehouse supplies) (¶192) shipping clerks' salaries, warehousemen's wages and expenses (*warehouse labor), and other similar supplies. (¶198)

145. Credit purchases account,—

e. For all goods returned by us after having been purchased, and debited to purchases account.

f. For all **rebates and allowances* on purchases, such as shortage, damage or overcharge claims allowed on goods purchased when the full amount has been debited to purchases account, (¶206) or for *any rebates or returns on freight, express or other charges paid.

g. For goods taken from stock for private use or donation, *at cost price.*

h. For goods taken from stock to be shipped for sale on commission, or transferred to a branch store, when billed *at cost price.*

i. For any returns from material or labor debited to this account.

j. For †cash discounts allowed to us on purchases, when**purchase discounts* are considered as *decreasing the cost of purchases.*

**Unless subsidiary accounts are kept.* (¶152, ¶176)

†If considered as an income from having sufficient capital to discount bills (¶220*b*).

146. **Observe** that in every instance the purchases account is debited for something that *adds to or increases the cost of purchases:* or whatever *increases* costs is a debit.

147. **Observe** that in every instance the purchases account is credited for something that *decreases or lowers the cost of purchases:* or whatever *decreases* costs is a credit.

148. Transactions Illustrating the Various Applications of the Rule (¶ 142) for Debiting and Crediting Purchases Account

F. A. Raymond's transactions affecting the purchases account are as follows: Jan. 5. He paid freight charges, $10.15. (¶144*b*) – – Jan. 9. He paid a com-

mission of 1% and other expenses, amounting to $5.50, for goods purchased in New York through an agent. (¶144*c*) – – JAN. 12. He was allowed a shortage claim, $2.20. (¶145*f*) – – JAN. 14. He was allowed a rebate for an overcharge on freight paid, $1.60 (¶145*f*) – – Jan. 16. He was allowed a credit for an overcharge on goods purchased, $18.40. (¶145*f*) – – JAN. 18. He received an allowance for damaged goods purchased, $5.20. (¶145*f*) – – JAN. 25. He returned goods which were found to be unsalable, amounting to $40.16. (¶145*e*) – – JAN. 28. He paid freight, express and drayage bills, amounting to $27.85. (¶144*b*, ¶180.) – – JAN. 31. His purchase discounts for the month were shown to be $173.51. (¶145*j*) He paid salaries and wages for warehouse labor for the month, $120. (¶144*d*) He paid for boxes, packing and shipping material and other warehouse supplies for the month, $61.35. His total purchases for the month, as shown by the purchase book, were $3180.53 (¶144*a*)

What is the net cost of the merchandise purchased?

EXERCISE.

148*a*. Prepare a ledger account for the preceding transactions, as follows:

(**1**) Read and study each transaction carefully, referring to the special application of the rule for debiting and crediting purchases account indicated by the paragraph numbers. (¶145*g*, ¶145*h* and ¶145*i*, will be illustrated in subsequent exercises.)

(**2**) Apply the rule (¶142) and make the proper debit and credit entries in the purchases account, indicating in the explanation column the nature of each item, as shown in the illustration. When completed, submit for approval.

ILLUSTRATION 22.

Purchases

19				19			
Jan.	5	Freight	10 15	Jan.	12	Shortage	2 20
	9	Agents Comsets	5 50		14	Fr. rebate	1 60
	28	Freight etc.	27 85		16	Overcharge	18 40
	31	Warehouse labor	120		18	Damaged goods	5 20
	31	Warehouse supplies	61 35		25	Goods rtds	40 16
	31	Purchases 31643	3180 53		31	Purchase Discts.	173 51
			3405 53				241 07

148*b*. The illustration shows the account as it appears January 31, with the figures in the posting columns omitted. The small pencil figures show the footings, and also the balance of the account. This illustration shows the account as it appears when all the various charges and allowances affecting purchases are entered in one account, consequently, the balance shows the *net cost of merchandise purchased*. (¶149*a*) The account is not ruled nor footed until after the closing journal entry is posted, when the account would appear, after it is closed, as shown in illustration 23.

ILLUSTRATION 23.

31	Warehouse supplies	61 35	25	Goods rtd.	5 20
31	Purchases 3164.31	3180 53 (3405 38)	31	Purchase Discts.	173 51 (179 07)
			31	Trading a/c to close	3164 31
		3405 38			3405 38

148*c*. The illustration following shows the purchases account as it appears when *subsidiary* accounts are kept with warehouse supplies (¶192), warehouse labor (¶198), and purchase discounts (¶220), in which case the difference between the two sides of the account, $3156.47, shows the *first* or *prime cost*. (¶149*b*)

ILLUSTRATION 24.

Purchases

19					19			
Jan.	5	Freight	10 15		Jan.	12	Shortage	2 20
	9	Agents com. etc.	5 50			14	Frt. rebate	1 60
	28	Freight etc.	27 85			16	Overcharge	18 40
	31	Purchases 3156.47	3180 53 (3224 03)			18	Damaged goods	5 20
						25	Goods rtd.	40 16 (45 63)
						31	Trading a/c to close	3156 47
			3224 03					3224 03

148*d*. Notice that the balance shown by this account differs from the balance shown by the preceding account. This is caused by the elimination of the three items of warehouse labor, warehouse supplies, and purchase discounts, which are shown in separate accounts and will appear as separate items in the trial balance. The balance of this account *is the one shown in the trial balance.* (¶483).

To Close Purchases Account.

149. The difference between the two sides of the purchases account always shows a debit balance, which should be included in the trading statement for the period. (¶242). (*a*) If all the various charges and allowances affecting purchases are entered directly into the purchases account, the balance shows the *net cost of merchandise purchased.* (¶148*b*) (*b*) If subsidiary accounts are kept for accounts named in ¶144*d* and ¶145*j*, the balance shows the *first* or *prime cost* of the goods purchased. (*c*) If subsidiary accounts are kept with all the various charges and allowances affecting purchases excepting items named in ¶144*a* and ¶145*e*, the balance shows the *net invoice price* of the goods purchased for the period.

150. To close. After the trading statement has been prepared, the purchases account is closed by a journal entry made up from the items appearing in the trial balance which affect the trading statement. When the closing item to the purchases account has been posted, which should balance the account, rule the closing lines in red ink, as shown in illustration 23, and enter the footings in black ink.

151. It is the best practice to enter the items coming under ¶144*a* and ¶144*b*, i. e., for goods purchased per invoices and for transportation and other charges thereon, directly into the purchases account. It is also the best practice to enter the items coming under ¶145*e*, ¶145*g*, ¶145*h* and ¶145*i*, i. e., those items for goods returned, for goods taken from stock, and for rebates on transportation charges, directly in the purchases account. This practice is preferred for the reason that in preparing the trading statement these items can easily be separated one from the other in the ledger account, particularly if each item is designated in the explanation column as entered. All the items included in ¶144*a* to ¶145*j* may be entered directly into the purchases account, particularly if the business is small.

152. Separate accounts for the items named in ¶144*b*, ¶144*c*, ¶144*d*, ¶145*f*, ¶145*i* and ¶145*j*, and other similar items relating to the purchases account may be kept when it is desired that they should appear separately in the trading statement and are so numerous as to make the method suggested in ¶153 impracticable. All such accounts are known as *subsidiary* purchase accounts.

153. When it is desired to show separately in the trading statement any one or more of the items included in ¶144*a* to ¶145*j*, inclusive, whether entered in the principal purchase account or in subsidiary accounts, they may be separated on an *analysis sheet* to whatever extent is desired, at the time of preparing the trading statement. The analysis sheet is described in ¶490. The analysis sheet is preferred by many accountants because by its use the number of accounts in the ledger may be greatly reduced, the trial balance shortened, and the opportunities for errors lessened.

Exercises in Purchase Accounts.

154. Prepare ledger accounts, like the illustration 22, for the following examples, applying the rule (¶142) for each transaction, following carefully the special instructions for each example. Indicate briefly in the explanation column the nature of each item.

(**1**) Jan. 4. Paid freight and drayage on purchases, $157.13 (¶144*b*); storage charged by railroad, $2.00. – – Jan. 6. Received credit memorandum for defective goods returned, $46.17 (¶145*f*) – – Jan. 8. Received credit memorandum for shortage in goods purchased, $12.20. – – Jan. 18. Merchandise was taken from stock for the private use of the proprietor, at cost, $6.70. – – Jan. 21. He donated goods to the Salvation Army, at cost price, amounting to $10. – – Jan. 31. The Merchants' Transfer Co's bills for drayage for the month amount to $17.50. Shipping boxes were purchased to the amount of $42; nails, $1.00; salaries of warehousmen and packers, $80; purchase discounts, $116.40. The total purchases for the month shown by the purchase book, were $2316.19.

What is the net cost of the merchandise purchased for the month? (¶149*a*) Show the account as it would appear Jan. 31, with the columns footed and the balance shown in pencil. When approved, enter the difference on the smaller side under date of Jan. 31, writing "Trading % to close" in the explanation column, as shown in illustration 23, then rule and foot the account and present it for approval.

(**2**) The following items are shown in the purchases account under date of April 30:

Purchases for the month, $16,936.17; freight and drayage inward, $116.24; purchasing agent's salary, one month, $125; traveling expenses to Boston, New York and Philadelphia, buying goods, $145.87; boxes and crates purchased for the month, $36.14; shipping clerks' salaries and warehousemen's wages, $120; credits received for goods returned, $45.16; rebates and allowances, $27.18; merchandise transferred to branch store, at cost, $269.14; received check from railroad company for $27.16 for overcharges on freight during the month; purchase discounts, $276.19.

Prepare the account showing the net cost of merchandise purchased, with the account closed, ruled and footed as previously instructed. What is the net invoice price of the goods purchased (¶149*c*)? the first or prime cost (¶149*b*)? Remember that in keeping a set of books the closing entry, "April 30 Trading % to close," would not be made until posted from the journal. (¶150)

155. The results shown by accounts supply the material of so many arithmetical problems, each one of which is solved by ordinary arithmetical processes. The facts or results shown by any account may be stated in the form of an ordinary problem in arithmetic, as shown in the following examples and illustration. One of the principal functions of accounting is putting arithmetical results into the form of statements so that these results may be shown in their proper relations.

Arithmetical Problems—Purchases Account.

(**1**) During the month of May the purchases were $7619.76; freight inward, $217.86; storage and drayage, $56.17; lumber for boxes, $26.10; nails, $4.00; paper and twine, $2.60; shipping clerks' salaries, $96; warehousemen's wages, $18; purchasing agent's salary, $125; traveling expenses, $28.60; credit memorandum received for goods returned, $16.40; allowances for overcharges on bills, $21.36; received for claim allowed by railroad for goods damaged in transit, $8.60; merchandise sold to employes at cost, $28.90; donation of goods to Orphans' Home, $30; goods shipped to Babbitt & Co. on commission, at cost, $105.30; purchase discounts, $217.64.

What was the net cost of the merchandise purchased for the month?

Illustration 25.

Solution

Costs	Deductions
7619.76	16.40
217.86	21.36
56.17	8.60
26.10	28.90
4.	30.
2.60	105.30
96.	217.64
18.	428.20
125.	
28.60	
8194.09	Total costs.
428.20	Deductions.
7765.89	Net cost.

(**2**) Purchases for the month, $11613.20; freight, express and drayage charges, $271.12; credit received for overcharge on freight bill, $13.97; duties on goods imported, $114.36; boxing, packing and shipping materials, $68.97; credit received for allowance caused by defective packing, $12.90; goods returned, $41.50; goods shipped for sale on commission, at cost, $312.17; cash discounts allowed on purchases, $293.43.

What is the net cost of the goods purchased for the month?

(**3**) Total purchases for the year ending December 31, $87963.43; total cost of freight, express, drayage, duties, storage, and other charges for the year, $5537.36; goods taken from stock for private use, at cost price, $91.20; goods shipped for sale on commision, at cost price, $962.50; rebates on transportation charges, $31.12

What is the first, or prime, cost of the purchases for the year? (¶149*b*) What item in the above problem represents the net invoice price of the goods purchased for the year? (¶149*a*)

(**4**) Purchases for month, per purchase book, $3167.19; incoming freight and drayage, $76.18; duties and storage, $56.12; commission for buying, $100; purchasing agent's expenses, $9.60; allowances and shortages, $34.20; shipments to Day & Co. at cost, $180; transferred goods to Rich street branch store at cost, $236.17; the Transfer & Storage Company allows us a credit of $6.45 for overcharges and errors in their bills of this month; purchase discounts during the month, $196.14; salaries of boxers and packers, $95; lumber, $20; twine, $1.50; wrapping paper, $12; nails, $1.50; strap iron, $3; excelsior, $2.75.

What is the net invoice price, prime cost, and net cost of purchases for the month? (¶149)

SALES ACCOUNT—A PRINCIPAL TRADING ACCOUNT.

156. The object of the sales account is to show the *returns from sales* (proceeds) for the period covered by the account. The *credit* side of the account shows the *gross sales*, from which is deducted the value of any goods returned, of allowances, rebates, overcharges, and of any other items that have the effect of *reducing the returns from sales*, these items appearing on the *debit* or *contra* side of the account.

Rule for Debiting and Crediting Sales Account.

157. *Debit for costs: credit for returns.*

157*a*. Debit sales account for goods returned to us, and for rebates and allowances to others on sales.

157*b*. Credit sales account for the *gross sales* of merchandise.

158. The various applications of the rule are as follows:

159. Debit sales account,—

a. For all goods returned to us after having been sold and credited to sales account.

b. For all **rebates and allowances* on sales, such as shortage, damage, or overcharge claims allowed on goods sold when the full amount has been credited to the sales account. (¶210)

c. For† cash discounts allowed to others on sales when **sales discounts* are considered to be a *reduction in return from sales*. (¶266)

160. Credit sales accounts,—

d. For all merchandise sold.

e. For goods taken from stock to be shipped for sale on commission, *when billed at selling price*.

**Unless subsidiary accounts are kept.* (¶176)

†If considered an expense from not having sufficient capital. (¶226*b*)

161. **Observe** that in every instance the sales account is debited for something that *diminishes or decreases the returns from sales:* or whatever *decreases* returns is a debit.

162. **Observe** that in every instance the sales account is credited for something that *adds to or increases the returns from* sales: or whatever *increases* returns is a credit.

163. Transactions Illustrating the Various Applications of the Rule (¶157) for Debiting and Crediting Sales Account

F. A. Raymond's transactions affecting the sales account are as follows:

Jan. 19. He allowed an overcharge claim of $7.56. (¶159*b*) – – Jan. 21. He allowed for goods damaged by careless packing, $12.40. (¶159*b*) – – Jan. 25. He allowed a shortage claim of $15.18 for goods which were omitted from the shipment by a mistake. (¶159*b*) – – Jan. 31. The total amount of goods returned for credit during the month was $64.13. (¶159*a*) – – The sales discounts for the month were shown to be $171.64. (¶159*c*) – – His total sales for the month, as shown by the sales book, were $7124.38. (¶160*d*)

What were the net returns from the merchandise sold? (¶164)

EXERCISE.

163*a*. Prepare a ledger account for the preceding transactions, as follows:

(1) Study each transaction carefully, looking up the references indicated by the paragraph numbers.

(2) Apply the rule (¶157) and make the proper debit and credit entries in the sales account, indicating in the explanation column the nature of each item, as shown in the illustration. Then foot the account, enter the difference on the lesser side with the explanation, "Trading a/c to close," rule the account, and bring down footings. When completed, present for approval.

ILLUSTRATION 26.

Sales

19				19				
Jan.	19	Overcharge	7 56	Jan.	31	Sales	6853.47	7124 38
	21	Damaged goods	12 40					
	25	Shortage	15 18					
	31	Goods rtd.	64 13					
	31	Sales Discts.	171 64					
	31	Trading a/c to close	6853 47					
			7124 38					7124 38

163*b*. The illustration shows the account when all the various charges affecting sales are entered in one account, including sales discounts (¶226) which are usually entered in a separate account. The illustration below shows the account with this item omitted, which appears in a subsidiary account considered as a trading account (¶226*a*). The first illustration shows the account as it appears when the trial balance is taken, the balance in pencil figures being shown in the trial balance (¶483). The second illustration shows the account after the closing entry has been posted and the account has been ruled and footed.

ILLUSTRATION 27.

Sales

19				19				
Jan.	19	Overcharge	7 56	Jan.	31	Sales	7025.11	7124 38
	21	Damaged goods	12 40					
	25	Shortage	15 18					
	31	Goods rtd.	64 13					
	31	Goods rtd.	64 13					
	31	Trading a/c to close	7025 11					
			7124 38					7124 38

TO CLOSE SALES ACCOUNT.

164. The difference between the two sides of the sales account always shows a credit balance, which should be included in the trading statement for the period

(¶242). (*a*) If all the various charges and allowances affecting sales are entered directly into the sales account, the balance shows the *net returns from merchandise sold* for the period. (*b*) If subsidiary accounts are kept with all the various charges and allowances affecting sales excepting items named in ¶159*a* and ¶160*d*, the balance shows the *net sales* for the period.

165. To close. After the trading statement has been prepared, the sales account is closed by a journal entry made up from the trading statement. When the closing item to the sales account has been posted, which should balance the account, rule the closing lines in red ink, as shown in illustrations 26 and 27, and enter the footings in black ink.

166. *It is the best practice* to enter the items coming under ¶160*d*, ¶160*e*, and ¶159*a*, being the items of goods sold and of goods returned, directly into the sales account, as these items, if they are required to appear as separate items in the trading statement, can easily be classified on an analysis sheet, particularly if each item is designated in the explanation column as entered.

167. *Separate accounts* for the items named in ¶159*b*, ¶159*c*, and other similar items relating to the sales account (excepting those named in ¶166) may be kept when it is desired that they should appear separately in the trading statement. When kept, these are known as *subsidiary* sales accounts.

Exercises in Sales Accounts

168. Prepare ledger accounts like illustration 26 for the following examples, applying the rule (¶157) for each transaction, indicating briefly in the explanation column the nature of each item. Include the entry "Trading % to close" which would be made from the closing journal entry in keeping a set of books.

(**1**) June 7. Goods were returned, $78.25. – – June 11. Rebate was made for overcharge, $62.56. – – June 30. Total sales were $8619.71; cash discounts during the month $208.16.

What are the net returns from merchandise sold?

(**2**) July 10. Goods were shipped on consignment at selling price, $367.19. – – July 21. Goods were returned, $116.42, and an allowance of $10 for an overcharge was made. – – July 27. Claim for damaged goods was allowed, $7.21. Sales discounts, $316.43; total sales, $9716.73.

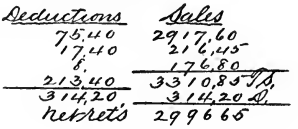
What were the net returns from sales?

Arithmetical Problems—Sales Accounts.

Find the results for the following problems (¶155):

ILLUSTRATION 28.

(1) During the month of August the sales on account were $2917.60; sales for cash, $216.45; goods shipped on consignment at selling price, $176.80; goods returned, $75.40; allowances for overcharges, $17.40; allowance for goods damaged on account of defective boxing, $8.00; sales discounts, $213.40.



(2) Sales on account for the month, $7916.70; cash sales, $219.67; sales account credited for undercharges on goods previously billed, $20; goods shipped on consignment at selling price, $276.18. Of this shipment, goods were returned amounting to $176, there being no market for them at the point to which they were shipped. Goods returned, $27.16; various allowances and rebates, $38.40; sales discounts, $3.16. What are the net returns from sales?

(3) Total sales, $4713.75; goods returned, $96.18. With separate accounts kept for items included in ¶159*b* and ¶159*c*, what are the net sales for the month? (¶164*b*) If there were rebates and allowances amounting to $84.12, and cash discounts amounting to $53, what were the net returns from sales? (¶164)

INVENTORY ACCOUNTS.

169. A merchandise inventory is a list of merchandise in stock or on hand at the end of any fiscal period taken at *cost price*, or if market price is less than cost, then at *market price*. The cost price of each article in an inventory is the invoice price plus a proportionate share of freight, express, and other charges and expenses necessary in placing the article in stock. These incidental charges should be and usually are figured in the *marked cost price* placed upon the article when it is received. They correspond with the debit items charged to the purchases and subsidiary accounts exclusive of the invoices. It is upon the marked cost price that the percentage of profit is added in fixing the *selling price*. When certain fixed discounts, such as trade discounts, are to be allowed, which are to be excluded from the percentage of profit, they are added to the selling price, in which case the price placed upon the goods is the *marked selling price*.

169*a*. *Shop-worn goods, goods out of style or out of date*, should be inventoried at cost, and the amount of the depreciation between the *cost* value and the *estimated* value should be listed separately. The total amount of the depreciation should be charged in the profit and loss statement as a separate item, otherwise the trading profit shown by the trading statement would be affected, which would thus disturb the average per cent of gross profit when the trading profit of one period is compared with that of another.

170. It should be remembered that a merchandise inventory should include only the value of goods on hand which were purchased to be sold at a profit, and that the inventory should not include the value of furniture and fixtures, office appliances, machinery, warehouse implements, boxing and packing materials, or any other

property whatsoever except that included in the designation, "purchased to be sold at a profit."

171. The object of the merchandise inventory account is to show the value of the merchandise on hand at the end of any fiscal period. The inventory account shows a *resource*, which should be included in the statement of resources and liabilities for the period, and is, therefore, known as a *resource* or asset account.

Rule for Debiting and Crediting Inventory Accounts.

172. *Debit* for the value of the inventory on hand *at the end of any fiscal period*: *credit* for the inventory on hand *at the close of the last preceding fiscal period.*

172*a*. Note that the inventory account is debited for the value of the inventory on hand *at the end of any fiscal period.*

172*b*. Note that the inventory account is credited at the close of the next fiscal period for the inventory for which it was debited *at the the close of the last preceding fiscal period.*

172*c*. Other inventories are described in ¶465.

173. Transactions Illustrating the Merchandise Inventory Account.

The following are monthly inventories covering a period of three months prior to January 31. Prepare a ledger account showing them properly debited and credited:

October 31, $6842.19; November 30, $8716.42; December 31, $7516.45;

Illustration 29.

Inventory

19 Oct.	31		6842 19	19 Nov.	30		6842 19
Nov.	30		8716 42	Dec.	31		8716 42
Dec.	31		7516 45				

173*a*. Notice that the account is debited for the inventory of October 31 on that date, and that the account is credited for the same inventory on November 30, one month later when the next inventory is taken, at which time the balancing items are ruled out as shown; and that, therefore, the account will always show the value of the merchandise on hand *at the close of the last preceding fiscal period.*

174. The inventory of the last preceding fiscal period, added to the cost of the purchases for the present fiscal period, less the inventory for the present fiscal period, gives the cost of the merchandise sold. (See trading statement, ¶242).

LLUSTRATION 30.

INVENTORY DECEMBER 31, 19 .

2488 bu.	Wheat	.97	2413.36
5674 "	Oats	.51	2893.74
765 "	Rye	.83	634.95
2624 "	Corn	.60	1574.40
			7516.45

Exercises in Inventory Accounts.

175. Prepare accounts for the following transactions:

(1) At the closing of the books, December 31, the inventory of goods on hand was $11360.50. – – At the next semi-annual closing, June 30, the inventory was $12448.37. – – At the next semi-annual closing, December 31, the inventory was $10991.71. What does the account show at that date?

(2) In a business where quarterly inventories were taken, the inventory on March 31 was $23741.49, on June 30, $64927,26, on September 30, $64417.71, and on December 31, $45516.85.

Show the account as it would appear December 31.

Arithmetical Problems—Inventory Accounts.

(1) The inventory at the close of the last preceding fiscal period was $2396.45. – – The net cost of merchandise purchased for the present fiscal period is $14365.27. – – The inventory at the close of the present fiscal period is $2875.90

What is the cost of the merchandise sold during the present fiscal period? (¶174)

Illustration 31.

Solution

2396.45 Pres. Invt.
14365.27 Purchases
16761.72 Total cost
2875.90 Pres. Invt.
13885.82 Cost of Merch. sold.

(2) The last preceding inventory was $96784.00. – – The total purchases for the fiscal period are $263712.37. – – The present inventory is $87979.12.

What is the cost of the merchandise sold during the period?

(3) The last preceding inventory was $61320. – – There were no purchases since. – – The present inventory is $9721.12

What is the cost of the merchandise sold?

(4) The business was started at the beginning of the present fiscal period with no inventory on hand. – – The total purchases to date are $35712. – – The present inventory is $7420.

What is the cost of the merchandise sold?

SUBSIDIARY TRADING ACCOUNTS.

176. The subsidiary accounts include all accounts, other than the principal trading accounts, which contribute towards *increasing* or *diminishing* the *gross trading profit*. They are kept for the purpose of classifying, under separate heads, the various items affecting the purchases and sales accounts which would otherwise be entered directly into those accounts, so that they may be shown separately, if desired, in the trading statement.

177. Subsidiary accounts vary considerably in different lines of business, depending upon the nature and extent of the business, the amount of detailed information desired, and, to some extent, upon the frequency with which similar items occur.

178. The usual disposition of subsidiary items is indicated in paragraphs 151, 152, 153, 166 and 167, although this arrangement may not be the best in all cases. In preparing a system of accounts for any line of business, the exact information required must first be determined and then the accounts must be so arranged as to provide that information. In the sets accompanying this text various arrangements of subsidiary items and accounts are illustrated, each being the one best adapted to give the information desired for the particular line of business illustrated.

179. All subsidiary items may be entered directly into the purchases and sales accounts, in which case it is necessary to separate them into classes or groups, under appropriate headings, on separate sheets or statements, before a detailed trading statement can be prepared. These are known as *analysis sheets* or "exhibits" (¶490) and they are attached to and accompany the trading statement. This method is particularly well suited to departmental accounts.

FREIGHT.

180. Freight and express charges are the amounts paid for the transportation of goods by public carriers. Drayage and cartage charges represent the cost of hauling goods between the warehouse and shipping points. As understood by accountants, the term "freight" includes all freight, express, drayage, cartage, and other charges relating to the transportation of goods.

181. The terms on which goods are bought and sold, generally indicate which of the parties is to pay transportation charges. Goods shipped "f. o. b." (free on board) means that the seller delivers the goods on board the cars, boat or ship, after which they are transported at the expense of the buyer. "Charges prepaid" generally means that the seller of goods shipped f. o. b. pays the freight or express charges at the point of shipment for the buyer, and that the buyer becomes indebted to the seller for the amount. Goods shipped "f. o. b. delivery point" means that the seller is to pay the carrying charges; if they are paid by the buyer the seller becomes indebted to him for the amount. However, in any case *it is a matter of agreement be-*

tween the parties when the sale is made as to who is to bear the expense of the transportation charges.

182. There are two kinds of freight. *Incoming* freight (or "freight in") relates to charges on goods purchased. *Outgoing* freight (or "freight out") relates to charges on goods sold.

183. "Freight In" *increases the cost of goods purchased* and is generally charged direct to the purchases account, no separate account being kept, *which is the best practice.* "Freight" or "Freight Out" is the heading generally used where a separate account is kept for freight charges on goods sold, which are *selling expenses* and do not relate to purchases account. (This account is treated in detail in ¶278).

"FREIGHT IN" ACCOUNT.

184. If for any reason a separate account for "freight in" is kept, it will show (1) the cost of freight, express and drayage charges paid on goods purchased (¶144*b*), (2) the amount (if any) of these charges rebated and returned (overcharges, mistakes in rating, etc.) (¶145*i*), and (3) from these the net *increase of cost* to the purchases account in the trading statement is ascertained, which is shown by the *difference* between the two sides of the account, which should always show a debit balance.

RULE FOR DEBITING AND CREDITING "FREIGHT IN" ACCOUNT.

185. *Debit for costs: credit for returns.*

186. The various applications of the rule are as follows:

187. Debit **freight in** account.

a. For all freight, express or drayage charges paid by us on incoming goods. (¶144*b*)

b. For all freight, express and drayage bills paid by others for our account on incoming goods. (¶144*b*)

188. Credit **freight in** account.

c. For all rebates or other returns on charges previously debited to this account. (¶145*i*)

d. For all freight or express bills paid by us for others which have been charged to this account. (¶145*f*)

As this account is seldom kept, it is not illustrated.

189. The difference between the two sides of "Freight In" account shows a debit balance, which is *added to the cost of purchases* in the trading statement.

190. To close. After the trading statement has been prepared, this account is closed by a journal entry which is made up from the items appearing in the trading statement. When the closing item for this account has been posted, which should balance it, then rule the closing lines in red ink and enter the footings in black ink, as shown in other similar accounts.

WAREHOUSE ACCOUNTS.

191. After goods are received there are two classes of items which enter into the cost of handling the goods while in our possession (i. e., up to the time they are ready for delivery to customers or on board cars) which add to the cost of purchases, (1) those showing the cost of boxes, cases, crates, packing materials, shipping tickets, and other items used in preparing the goods for shipment, and (2) those showing the cost of the labor employed. (¶144*d*) Separate accounts are usually kept although both classes of items may be included in one account under the heading of "Warehouse Expense," in which case the details may be shown to whatever extent required on an analysis sheet, or they may be charged directly to purchases account. When separate accounts are kept they may be designated as *warehouse supplies* and *warehouse labor*.

WAREHOUSE SUPPLIES ACCOUNT.

192. The object of this account when kept (¶152) is to show the cost of shipping materials of every description used in preparing the goods for market up to the time they are ready for delivery, which *increases* the cost of the merchandise sold in the trading statement.

Rule for Debiting and Crediting Warehouse Supplies Account.

193. Debit the account *for the cost of all materials used in preparing goods for market up to the time they are ready for delivery.* (¶144*d*) Credit the account *for any deductions or rebates from the cost, or for the value of materials taken from the account.* (¶145*i*)

194. Transactions Illustrating the Application of the Rule.

(1) F. A. Raymond's transactions for the month of January affecting the warehouse supplies account were as follows:

Jan. 6. He purchased boxes amounting to $10.50. – – Jan. 9. He purchased lumber for the making and repairing of boxes, $8.40. – – Jan. 10. He paid for nails, etc., $1.65. – – Jan. 15. He paid for wrapping paper, $6.40. – – Jan. 20. He purchased boxes for $22.40. – – Jan. 26. He purchased lumber amounting to $13.10. – – Jan. 27. He secured a rebate of $1.10 on bill for boxes purchased Jan. 20.

What was the cost of the warehouse supplies for the month?

(1) Trace each transaction in the illustration shown below.

(2) Prepare a ledger account like the illustration, inserting the closing entry for the item $61.35, as shown in the illustration. Rule the account, foot and present for approval.

ILLUSTRATION 32.

Warehouse Supplies

19				19			
Jan.	6	Boxes	10 50	Jan.	19		
	9	Lumber	8 40		31	Trading a/c, to close	61 35
	10	Nails	1 65				
	15	Wrapping paper	6 40				
	20	Boxes	22 40				
	26	Lumber c.o.s.	13 10				
			62 45				62 45

194*a*. Remember that the closing entry, "Trading a/c to close", on January 31, is inserted in the exercises merely to show the account closed. In keeping a set of books, this entry would not be made until it was posted from the journal. (¶196). Naming the items debited and credited in the explanation column assists in understanding the account, and particularly in analyzing it, if such should be necessary. The names of the items are frequently omitted, however, in subsidiary accounts.

To Close Warehouse Supplies Account.

195. The difference between the two sides of this account will show a debit balance, which is added to the *cost of purchases* in the trading statement. (¶242)

196. To close. After the trading statement has been prepared, this account is closed by a journal entry which is made up from the items appearing in the trading statement. When the closing item for this account has been posted, which should balance it, then rule the closing lines in red ink, as shown in illustration 32, and enter the footings in black ink.

196*a*. Resource and liability inventories affecting this account are explained in ¶465.

Exercises in Warehouse Supplies Accounts.

197. Prepare ledger accounts like the illustration above for the following examples, applying the rule for each transaction, and present for approval.

(1) The Egbert Grocery Co.'s transactions affecting warehouse supplies account for April are as follows:

April 3. Boxes, $146.19. – – 9. Barrels, 8.00. – –11. Nails, $4.75. – – 14. Paper, $18.45. – – 15. Twine, $4.50. – – 18. Strap iron, $31.20. – – 24. Excelsior, $6.70. – – 29. Boxes sold to another merchant, $13.20.

How much has this account added to the cost of purchases for the month? (¶133, ¶149)

Arithmetical Problems—Warehouse Account.

(1) The Brown Mfg. Co. purchased the following warehouse supplies for the month:

Boxes, $151.50; lumber, $34; nails, $3.50; crates, $10.20; wrapping paper $22.16; twine, $5.00; strap iron, $21.60; excelsior, $9.50. – – They sold boxes and barrels, $9.60; returned wrapping paper below grade, $12.50.

To what extent has the cost of merchandise been increased?

(2) The Acme Glass Co. purchased boxes, $216.50; lumber, $2619.84; freight on lumber, $54.26; nails, $34; packing hay, $116.40; straw, $71.20. – – They received from the sale of boxes, $15.20. – – They used of the lumber, for repairs to the building, $45.20.

What is the net cost of the warehouse supplies for the month?

WAREHOUSE LABOR ACCOUNT

198. Labor in this connection means the wages of those employed in opening boxes, crates, or breaking large packages and putting them up into smaller ones, and such other duties as are required in filling the orders of customers or in putting goods in shape for the market. This account is usually kept to include the wages of shipping clerks, warehousemen, and all others employed in preparing and handling the goods up to the time they are ready for delivery to customers or for shipment.

199. The object is to show the *cost* of the labor employed in preparing goods for sale while in our possession, which *increases* the cost of purchases in the trading statement. (¶152)

Rule for Debiting and Crediting Warehouse Labor Account.

200. Debit the account *for the cost of the labor employed, i. e., salaries or wages of boxers, packers, assorters, or other persons assorting goods or filling orders.* (¶144*d*) Credit the account *for the value of any labor employed elsewhere.* (¶145*i*).

201. Transactions Illustrating the Application of the Rule.

(1) F. A. Raymond paid wages of shipping clerks and warehousemen as follows:

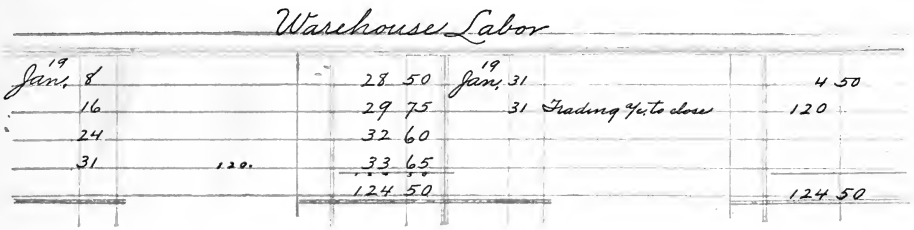
Jan. 8. $28.50; Jan. 16, $29.75; Jan. 24, $32.60; Jan. 31, $33.65. – – During the month one of the warehousemen was employed at various times in another department. His time was worth $4.50

What was the cost of the warehouse labor for the month?

(1) Trace each transaction in the illustration.

(2) Prepare a ledger account, inserting the closing entry for the item, $120.00 as shown in the illustration. Rule the account, foot, and present for approval.

ILLUSTRATION 33.



TO CLOSE WAREHOUSE LABOR ACCOUNT.

202. The difference between the two sides of this account will show a debit balance, which *increases the cost* of the goods purchased in the trading statement.

203. To close, read ¶196

EXERCISES IN WAREHOUSE LABOR ACCOUNTS.

204. Prepare ledger accounts for the following examples, applying the rule:

(1) B. F. Hudson's pay-roll included wages of boxers, packers, shippers, markers, etc., as follows: January 31, $250; February 28, $311.45; March 31, $350; April 30, $320; May 31, $216.65; June 30, $234.17. – – Labor charged to this account amounting to $37.65 was employed elsewhere.

How much was added to the cost of purchases for the half year?

ARITHMETICAL PROBLEMS—WAREHOUSE ACCOUNT.

(1) The pay-roll of the Sun Mfg. Company shows wages of boxers and packers as follows: January, $160; February, $175; March, $173.50; April, $119.75; May, $160.50; June, $148.75; July, $80; August, $87.50; September, $141.50; October, $137.50; November, $163; December, $121.50. – – The account was credited in April for $25, in September for $33, and in December for $16.50, being the wages of packers whose time was used for other purposes.

What was the net cost of the warehouse labor for the year?

REBATES AND ALLOWANCES

205. In the purchase and sale of goods, errors in price, in quantity, or in grade of goods frequently require adjusting entries. In some lines of business and under some circumstances the amounts of these adjustments should appear as separate items in the trading statement. These adjustments may properly be entered directly in the purchase and sales accounts (¶145*f*, ¶159*b*), and if it is desired to show them separately on the trading statement, they may be classified on an analysis sheet. When there are a sufficient number of these items to justify it, separate rebate and allowance accounts may be kept with both purchases and sales.

Purchase Rebates and Allowances Account.

206. The object is to group the rebate and allowance items on purchases under one heading in the ledger, instead of crediting them to purchases account and afterwards classifying them on an analysis sheet.

Rule for Debiting and Crediting Purchase Rebates and Allowances Account.

207. Read ¶145*f*. There are no debits to this account except for items wrongfully credited to it.

Note: As this account is in reality a part of the purchases account, which has already been explained and illustrated, no account is shown.

208. The difference between the two sides of the account will show a credit balance, which should be shown as an item *decreasing the cost of purchases* in the trading statement. (¶242)

209. To close, read ¶196

Sales Rebates and Allowances Account.

210. This account is in every respect similar to the purchase rebates and allowances account, except that the items have the effect of *reducing the returns from sales.*

211. The object is to group the rebate and allowance items on sales under one heading in the ledger instead of charging them direct to the sales account and afterwards classifying them on an analysis sheet.

RULE FOR DEBITING AND CREDITING SALES REBATES AND ALLOWANCES ACCOUNT

212. Read ¶159*b*. There are no credits to this account except for items wrongfully charged to it.

213. The difference between the two sides of the account will show a debit balance, which should be shown as an item *decreasing the returns from sales* in the trading statement.

MERCHANDISE DISCOUNTS.

214. A merchandise discount is a percentage deducted from a bill for its prepayment within a certain specified time from its date, which time is prior to the full term of credit allowed on the bill. It is in reality *the value of the use of the money for the time a bill is paid before it would otherwise be due,* which is calculated as a certain percentage of the bill, this percentage being deducted when payment is made.

215. The prepayment of a bill less discount is *optional with the purchaser* and, therefore, no entry is made in the books of the seller until payment is received. *It is optional with the seller* to allow the discount on a bill that is not paid until after the expiration of the term of discount. The "terms" of the bill generally indicate the full term of credit allowed on the bill and also the term of discount (if any), which is the limit of time from the date of the bill in which a discount may be deducted for its prepayment.

216. In practice, payment is usually made for the *difference* only between the face of the bill and the discount, but theoretically payment is made for the whole amount of the bill and the value of the discount is *returned* or paid back to the purchaser of the bill for the use of his money before it would otherwise have been paid.

217. Discounts are offered for the prepayment of bills, (*a*) to secure prompt payment of bills and consequently to secure the earlier use of money to carry on the business of the concern, and (*b*) to reduce the commercial risk in carrying the accounts of customers for a greater length of time. These discounts are known as *purchase discounts* and *sales discounts.*

218. What disposition should be made of purchase and sales discounts?

(*a*) Do purchase discounts decrease the cost of purchases and thus *increase* the gross trading profit, which would class them as *trading profits* to be shown in the trading statement, or (*b*) are they an income derived from having sufficient capital to discount bills, which would class them as a *capital income* to be shown in the profit and loss statement?

(*c*) Do sales discounts decrease the returns from sales and thus *decrease* the gross trading profit, which would class them as *trading losses* to be shown in the trading statement, or (*d*) are they expenses incurred to secure the earlier use of money and to reduce the risk of carrying accounts to their full maturity, which would class them as a *capital expense* to be shown in the profit and loss statement?

These are questions upon which there is considerable diversity of opinion among accountants, without much prospect of an early agreement as to which is the correct method of disposing of either.

219. In the absence of such agreement, all of these methods are illustrated in this work, so that either may be employed, depending upon the nature of the business and the wishes of the owner, which, after all, are important factors in determining which method should be followed.

PURCHASE DISCOUNTS ACCOUNT.

220. Purchase discounts are those which are allowed (or returned) to us for the payment of bills purchased.

220*a*. When purchase discounts are considered as *decreasing the cost of purchases*, they may be entered directly to the credit of purchases account (¶145*j*, ¶153) or a separate *purchase discounts* account may be kept, which is preferable. When so considered, purchase discounts account is classed as a *subsidiary trading* account, and the amount of the purchase discounts shown by it should appear in the trading statement as a *deduction from the cost of purchases*, which will *increase* the gross trading profit or *decrease* the gross trading loss shown by that statement

220*b*. When purchase discounts are considered as showing *an income derived from having the capital available to prepay bills*, a separate *purchase discounts* account should be kept, which is then classed as a *profit and loss* account, and the amount of the purchase discounts shown by it should appear as a profit in the profit and loss statement, as a separate item, which will *increase* the net profit or *decrease* the net loss shown by that statement.

Rule for Debiting and Crediting Purchase Discounts Account.

221. *Credit Purchase Discounts account for all discounts on bills prepaid by us.*

222. Observe that the account is credited for the *returns* to us for the use of money given in discounting our bills. Any debit items appearing in this account are simply *offset items* for credits to the account, for discounts which were not allowed to us. (¶215)

223. TRANSACTIONS ILLUSTRATING THE RULE FOR DEBITING AND CREDITING PURCHASE DISCOUNTS ACCOUNTS.

F. A. Raymond's transactions affecting purchase discounts for January are as follows:

JAN. 5. He was allowed a discount of $46.91; Jan. 12, $27.84; Jan. 19, $38.46; Jan. 27, $65.80. – – JAN. 20 he debited the account for $5.50, which he had deducted on a bill previously paid, which was not allowed.

What were the total discounts on purchases for the month?

(1) Trace each transaction in the illustration. The explanation column is left vacant, as all items are for discounts.

(2) Prepare a ledger account like the illustration, inserting the closing entry "Trading a/c to close," as shown in the illustration. (¶225*a*).

ILLUSTRATION 34.

Purchase Discounts

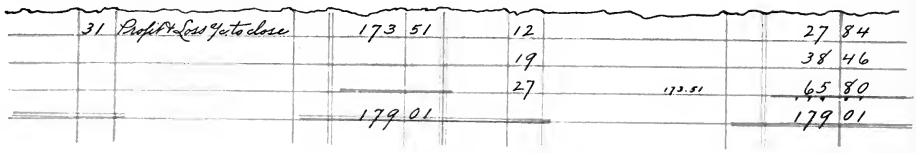
19				19		
Jan.	20		5.50	Jan.	5	46 91
	31	Trading a/c to close	173 51		12	27 84
					19	38 46
					27	65 80
			179 01			179 01

TO CLOSE PURCHASE DISCOUNTS ACCOUNT.

224. The object is to show the *total discounts on purchases.*

225. To close. (*a*) When considered as a subsidiary trading account *showing a decrease in the cost of purchases,* after the trading statement has been prepared, purchase discounts account is closed by a journal entry made up from the items appearing in the trading statement. When the item closing the account is posted, the explanation "Trading a/c to close" should be entered as shown in illustration 34. (*b*) When considered as a profit and loss account *showing an increase in the net profits,* after the profit and loss statement has been prepared, the account is closed by a journal entry made up from the items appearing in the profit and loss statement, in which case, when the item closing the account is posted, the explanation "Profit & Loss a/c to close" should be entered as shown in illustration 35. (*c*) In either case, when the closing entry for this account has been posted, which should balance it, rule the closing lines in red ink as shown and enter the footings in black ink.

ILLUSTRATION 35.



SALES DISCOUNTS ACCOUNT.

226. Sales discounts are those which we allow to others for the prepayment of bills we have sold.

226*a*. When sales discounts are considered as *decreasing the returns from sales*, they may be entered directly to the debit of the sales account (¶159*c*), or a separate *sales discounts* account may be kept, which is preferable. When so considered, sales discounts account is classed as a *subsidiary trading* account, and the amount of the sales discounts shown by it should appear in the trading statement as a deduction from sales, which will *decrease* the gross trading profit or *increase* the gross trading loss.

226*b*. When sales discounts are considered as showing *the cost of securing the earlier use of money*, a separate sales discounts account should be kept, which is then classed as a profit and loss account, and the amount of the sales discounts shown by it should appear as a loss in the profit and loss statement as a separate item, which will *decrease* the net profit or *increase* the net loss shown by that statement.

RULE FOR DEBITING AND CREDITING SALES DISCOUNTS ACCOUNT.

227. *Debit Sales Discounts account for all discounts on bills prepaid by others.*

228. Observe that the account is debited for the *cost* to us of discounts allowed on sales. Any credit items appearing in this account are simply *offset* items for debits to the account for discounts which were not allowed to others. (¶215)

229. TRANSACTIONS ILLUSTRATING THE RULE FOR DEBITING AND CREDITING SALES DISCOUNTS ACCOUNT.

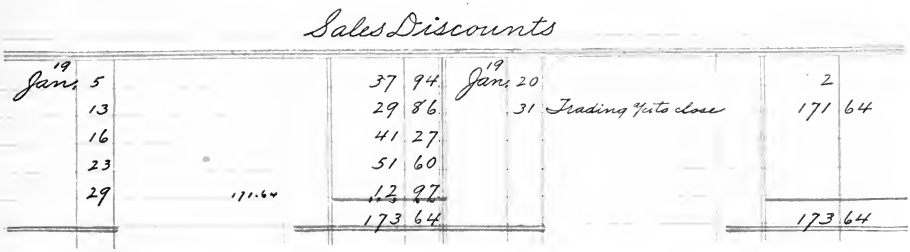
F. A. Raymond's transactions affecting sales discounts for January are as follows:

JAN. 5. He allowed a discount of $37.94; Jan. 13, $29.85; Jan. 16, $41.27; Jan. 23, $51.60; Jan. 29, $12.97. – – On JAN. 20 he found that he had allowed an over-discount of $2.00 on the item charged to sales discount account on Jan. 13.

What were the total discounts on sales for the month?

(**1**) Prepare a ledger account like the illustration, inserting the closing entry "Trading a/c to close," as shown in the illustration. (¶231*a*)

ILLUSTRATION 36.

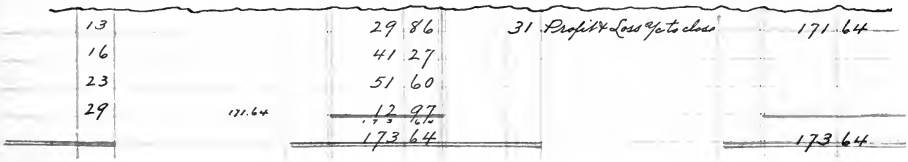


TO CLOSE SALES DISCOUNTS ACCOUNT.

230. The object is to show the *total discounts on sales.*

231. To close. (*a*) When considered as a subsidiary trading account *showing a decrease in the returns from sales,* after the trading statement has been prepared, sales discounts account is closed by a journal entry made up from the items appearing in the trading statement. When the item closing the account is posted, the explanation "Trading % to close" should be entered as shown in illustration 36. (*b*) When considered as a profit and loss account *showing a decrease in the net profits,* after the profit and loss statement has been prepared, the account is closed by a journal entry made up from the items appearing in the profit and loss statement, in which case, when the item closing the account is posted, the explanation, "Profit & Loss % to close" should be entered as shown in illustration 37. In either case, when the closing entry for this account has been posted, which should balance it, rule the closing lines in red ink as shown and enter the footings in black ink.

ILLUSTRATION 37.



Exercises in Purchase and Sales Discounts.

232. Prepare ledger accounts for the following examples, applying the rule, and present for approval.

(**1**) Jones & Co.'s purchase discounts, which were posted to the ledger account on the last day of each month, were as follows:

January, $317.45; February, $287.50; March, $411.16; April ,$275.76; May, $471.12; June, $386.45. – – March 10. A discount taken on a bill which was not paid until after the term of discount, was not allowed, $26.11. – – May 25. A similar discount was not allowed, amounting to $7.42.

What were the total discounts on purchases, and what result would it affect if considered as a subsidiary account to the purchases account? (¶220*a*) What result would it affect if considered as an income from capital? (¶220*b*)

(**2**) Brown Brothers allowed sales discounts for six months as follows:

July, $326.65; August, $512.62; September, $387.90; October, $216.65; November, $312.30; December, $516.80. – – Sept. 15. An error in calculating discount allowed was discovered, amounting to an over-allowance of $6.50. A similar over-allowance was discovered, November 23, of $3.65.

What were the total discounts on sales?

(**3**) The following transactions affecting purchase and sales discounts occurred during the month of April. (Open two accounts.)

April 3. Prepaid bill purchased, the discount amounting to $14.60. – – April 5. Allowed a discount on sale of April 2, $3.65. – – April 8. We prepaid a bill on which discount was $8.12 – – April 10. We allowed a discount for prepayment of bill sold, $13.45 – – April 18. We allowed a sales discount, amounting to $6.41 – – April 20. We allowed a sales discount of $3.66 – – April 23. We prepaid a bill purchased, saving a discount of $5.75 – – April 26. We saved a discount by prepaying bill purchased, $6.66 – – April 30. We allowed a sales discount, amounting to $4.50.

What were the Balances shown by the two accounts?

Arithmetical Problems—Purchase and Sales Discounts.

(**1**) The following purchase discounts were allowed us: January, $416.21; February, $213.20; March, $67.89. A discount amounting to $24.83, deducted after the term of discount had expired, was not allowed. What are the net purchase discounts allowed us for the three months?

2. We allowed the following sales discounts: July $89.98; August $114.96; September $342.25; October $211.88; November $401; December $740.01. In one of these discounts an error of $55 was discovered and charged back. Another error of $30 was charged back. What was the amount of sales discounts allowed to others?

THE TRADING STATEMENT.

233. This statement is made up from the *principal* trading accounts (i. e., the inventory, the purchases and the sales accounts) and the various *subsidiary* trading accounts. This group of accounts contains all the facts relating to the costs of, and the returns from the commodities bought and sold. These facts are arranged in systematic order in the statement with full explanations and not infrequently they are accompanied and supported by various supplementary exhibits such as analysis sheets, comparative statements, etc. (See illustration, ¶242)

233*a*. *The explanations and illustrations* of the trading statement, in this chapter relate to the trading statement and the accounts of an ordinary trading (mercantile or commercial) business in which merchandise is bought and sold for profit. The trading statement and special accounts of manufacturing and other lines of business will be treated later in this work.

234. The object of the trading statement is to show the *gross trading profit* or the *gross trading loss* from sales for the fiscal period represented (¶133). Any account which affects the gross trading profit or the gross trading loss resulting from the sale of merchandise properly belongs to and should be included in the trading statement.

235. The trading statement when properly made shows the *total cost of purchases* and also the *cost of merchandise sold* on the debit side against the *total* or *gross sales* and the *net returns from sales* (proceeds) on the other side.

236. The cost of purchases is found by adding to the inventory on hand at the close of the *last preceding fiscal period* the purchases for the present fiscal period and any other items shown on the debit side of the purchases account or by the subsidiary accounts relating to purchases that have *increased* the cost of purchases. From their sum, deduct all items shown on the credit side of the purchases account or by the sudsidiary accounts relating to purchases that have *decreased* the cost of purchases. The difference is the *net cost of purchases.* (See illustration ¶40.)

237. The cost of merchandise sold is the net cost of purchases *less the inventory at the close of the fiscal period,* which is shown in the trading statement by deducting the inventory from the net cost of purchases.

238. The returns from sales are found by adding to the gross sales for the present fiscal period, shown on the credit side of the sales account, any items shown on the credit side of subsidiary accounts relating to sales that have *increased* the total sales. From their sum deduct all items shown on the debit side of the sales account or by the subsidiary accounts relating to sales that have *decreased* the total sales. The difference is the *net returns or proceeds* from sales. "Net sales" is the differences between the *gross* sales and any deductions therefrom for goods returned, allowances, or other charges. See illustration 40.

239. The difference between the two sides of the trading statement, after deducting the inventory for the present fiscal period from the net cost of purchases on the debit side (or adding it to the credit side), represents the *gross trading profit* or the *gross trading loss* for the period.

239*a*. NOTE—The practice among American accountants is to deduct the closing inventory from the debit side in order to show as one item in the statement *the cost of the merchandise sold*, which is the best practice, because it is upon the cost of the goods sold that the *rate per cent* of the gross trading profit or loss is calculated. The English practice is to add the inventory to the credit side.

240. The trading statement is made up from the principal and subsidiary trading accounts shown in the final trial balance taken before closing the ledger. The trading accounts constitute one of the three groups of accounts contained in the trial balance of a commercial or trading business, as explained in ¶484.

241. The following is a list of the trading accounts and their balances as they appear in the trial balance shown in illustration 86, which is made up from the illustrative accounts contained in this text. It should be observed, however, that the balances shown by the various trading accounts do not always agree with the items shown in the statement, as the balances do not supply the detailed information required. In some instances, it is necessary to take the footings shown by each side of an account instead of the balances, and where various subsidiary items have entered directly into the purchases and sales accounts, if it is desired to show them separately in the trading statement, it is first necessary to classify and separate them on an analysis sheet. The analysis sheet is fully explained in ¶490.

ILLUSTRATION 38.

Purchases	3156 47	
Sales		7025 11
Inventory	7576 45	
Warehouse Supplies	61 35	
Warehouse Labor	120	
Purchases Discounts		173 51
Sales Discounts	171 64	

ILLUSTRATION 39.

INVENTORY JANUARY 31, 19 .

2148 bu.	Rye	.84	1804.32
4745 "	Oats	.51 1/2	2443.67
2482 "	Corn	.64	1588.48
			5836.47

242. The following illustration (40) shows the *report form* of the trading statement made up from the accounts contained in the section of the trial balance shown.

ILLUSTRATION 40.

Trading Statement January 31, 19 F. A. Raymond

Returns			
Gross Sales		7124 38	
Less - Rebates and allowances	35.14		
Goods returned	64.13	99 27	7025 11
Deduct - Sales discounts			171 64
Net returns from sales			6853 47
Costs			
Inventory December 31, 19		7516 45	
Purchases	3224.03		
Less - Rebates and allowances	27.40		
Goods returned	40.16 67.56	3156 47	
Add - Warehouse supplies		61 35	
Warehouse labor		120	
Total cost of purchases		10854 27	
Deduct - Purchase discounts		173 51	
Net cost of purchases		10680 76	
Less - Inventory January 31, 19		5836 47	
Cost of merchandise sold			4844 29
Gross trading profit			2009 18

PREPARATION OF THE TRADING STATEMENT.

RETURNS.

242*a*. Explanation. (¶233) The returns are shown first in this form (the report form) of the trading statement. (¶238).

(1) *Gross sales, $7124.38,* is the credit footing of the sales account (¶163*b*, ¶156). Refer to illustration 27, page 51. Read ¶241.

(**2**) *Rebates and allowances, $35.14,* is the sum of the three items on the debit side of the sales account (¶159*b*). If the sales account contained a considerable number of these items, they would be separated on an *analysis sheet* or separate account could be kept for them. (¶167). Refer to ledger account, illustration 27.

(**3**) *Goods returned, $64.13,* is found as a single item on the debit side of the sales account. When it is desired, they may be separated from any other items appearing on that side of the account as suggested in the preceding paragraph.

(**4**) *The gross sales* (7124.38) less the sum of the items for *rebates and allowances* and for *goods returned* (35.14 + 64.13 or 99.27) is the balance (7025.11) shown by the sales account which agrees with the trial balance.

(**5**) *Sales discounts, 171.64,* deducted from the balance of the sales account, gives the *net returns from sales, 6853.47.* (¶164*a*) If sales discounts were considered as a *capital expense* (read ¶220*b*), the item for 171.64 would be omitted from this statement, in which case the *net returns from sales* would be 7025.11, the balance shown by the sales account.

COSTS.

(**6**) (¶236) *Inventory, Dec. 31, 19—, 7516.45,* is the inventory of the "last preceding fiscal period." (¶174) See illustration 29.

(**7**) *Purchases, $224.03,* is the debit footing of purchases account (¶148*c* ¶140, ¶141). Refer to ledger account, illustration 24.

(**8**) *Rebates and allowances, 27.40,* and *goods returned, 40.16,* are exactly similar items to those explained in paragraphs 3 and 4, and are treated in the same manner except that they are deducted from *costs* instead of from *returns.* Their sum (67.56) deducted from the total purchases (3224.03) is 3156.47, the balance shown by the purchases account in the trial balance.

(**9**) *Warehouse supplies, 61.35,* and *warehouse labor, 120.00,* shown by those accounts, added to the other costs, give the *total cost of purchases, 10854.27. Purchase discounts, 173.51,* deducted gives the *net cost of purchases, 10680.76.* This amount, less *inventory, Jan. 31, 5836.47,* "the inventory for the present fiscal period," gives *cost of merchandise sold, 4844.29.*

(**10**) *The gross trading profit, 2009.18,* is the difference between the *net returns from sales, 6853.47,* and the *cost of merchandise sold, 4844.29.* (¶239).

(**11**) Prepare a trading statement like the one shown in illustration 40, following the explanation (¶242*a*) and present for approval.

Principles Involved in Making A Trading Statement.

243. Observe that the following principles apply in determining the gross trading profit or the gross trading loss:

(*a*) Any account or item that has *increased* the cost of purchases or *decreased* the returns from sales has *decreased* the gross trading profit or *increased* the gross trading loss.

(*b*) Any account or item that has *decreased* the cost of purchases or *increased* the returns from sales has *increased* the gross trading profit or *decreased* the gross trading loss.

EXPLANATION.

Illustrating principle 243a, note that the items for "warehouse supplies, 61.35," and for "warehouse labor, 120," amounting to 181.35, *increased* the cost of purchases and, therefore, *decreased* the gross trading profit by that amount; i. e., without these items the gross trading profit would have been 2190.53; note also that the items for "rebates and allowances, 35.14," and for "goods returned, 64.13," amounting to 99.27, *decreased* the returns from sales and, consequently, *decreased* the gross trading profit by that amount. The same is true of the item for "sales discounts, 171.64."

Illustrating principle 243b note that the items for "rebates and allowances, 27.40," and for "goods returned, 40.16," amounting to 67.56, *decreased* the cost of purchases and, therefore, *increased* the gross trading profit by that amount; note also that the same is true of the item for "purchase discounts, 173.51." There is no item that has "increased the returns from sales" shown in this trading statement.

244. The object of finding the gross trading profit is, (*a*) to ascertain whether or not the department of the business (mercantile or manufacturing) represented in the trading statement has been properly managed, as distinguished from the other departments of the business, such as the sales and administration departments, etc., (*b*) to permit of a comparison of the gross trading profit on sales of one fiscal period with that of another, and of other important facts, and (*c*) incidentally to prepare for finding the net trading profit.

245. Comparisons of the facts shown in a trading statement are usually made on a *percentage basis*. The percentages are found as follows:

(*a*) The gross trading profit (or loss) divided by the *cost of the merchandise sold* will give the *percentage of gross profit* (or loss) on sales.

(*b*) Any account or item that has increased or decreased the gross trading profit (or loss) divided by the gross trading profit (or loss) will give the percentage of the increase or decrease of the gross trading profit (or loss) caused by that account or item.

(*c*) The same is true of any group of accounts or items.

To Close Ledger Accounts Shown in the Trading Statement by Separate Journal Entry.

246. When the trading statement has been completed, a journal entry is prepared from the statement to close all the accounts in the ledger containing the items or balances shown in the statement, the *gross trading profit* or the *gross trading loss* appearing as one item in the entry to balance it, which is transferred to the proper side of the profit and loss account in the ledger.

247. The only purpose of closing the various accounts included in the trading statement is to *indicate the close of a business period,* and thus to *eliminate them as open accounts in the ledger,* preparatory to their receiving the entries of a new business period.

248. *Illustration 41* shows the correct journal entries to close the accounts included in the trading statement *when it is desired to open a trading account in the ledger.*

248*a*. *Debit trading accounts showing credit balances. Credit trading accounts showing debit balances. For inventories follow rule ¶172.*

Journal Entries When Trading Account is Opened in the Ledger.

Illustration 41.

January 31, 19

Sales a/c	To close	7025	11		
Inventory a/c	January 31, 19	5836	47		
Purchase Discounts a/c	To close	173	51		
Trading a/c				13035	09
	"				
Trading a/c		13035	09		
Sales Discounts a/c	To close			171	64
Purchases a/c	"			3156	47
Inventory a/c	December 31, 19			7516	45
Warehouse Supplies a/c	To close			61	35
Warehouse Labor a/c	"			120	
Profit & Loss a/c	Gross trading profit			2009	18

249. It will be noted that when the trading account is opened in the ledger it will be debited and credited for the same amount and, therefore, will balance. For this reason the trading account is frequently omitted from the ledger as an unnecessary account, in which case the two journal entries may be combined into one

by omitting the items debiting and crediting the trading account, as shown in the following illustration 42 of the preceding entries combined as one entry. The only objection to this method is that it is impossible to indicate the opposite account debited or credited in making the entry in the various ledger accounts. "Trading % to close" will overcome this objection.

ILLUSTRATION 42.

January 31, 19

Sales a/c	To close	7025 11	
Inventory a/c	January 31, 19	5836 47	
Purchase Discounts a/c	To close	173 51	
Sales Discounts a/c	"		171 64
Purchases a/c	"		3156 47
Inventory a/c	December 31, 19		7516 45
Warehouse Supplies a/c	To close		61 35
Warehouse Labor a/c	"		120
Profit & Loss a/c	Gross trading profit		2009 18

EXERCISES IN PREPARING TRADING STATEMENTS

250. Prepare trading statements for the following trading accounts as they appear in the various trial balances shown, and present for approval. The first example is an exact duplication, in form, of the trading statement shown in illustration 40, the only difference being in the amounts. These statements are prepared on ordinary journal paper, as shown in the illustration.

1. The section of A. W. Wilson's trial balance for December 31, 19 , containing the debit and credit items relating to trading accounts, is shown in the illustration below:

ILLUSTRATION 43.

Purchases	2963 19	
Sales		6755 29
Inventory — at close of last fiscal period	6981 46	
Warehouse Supplies	125 47	
Warehouse Labor	112 50	
Purchase Discounts		212 44
Sales Discounts	163 20	

ADDITIONAL INFORMATION REQUIRED TO PREPARE THE TRADING STATEMENT

In the above illustration, only the balances of the purchases and sales accounts are shown, whereas to give full information in the trading statement regarding

purchases and sales, as shown in illustration 40, reference must be made to the accounts in the ledger to obtain the amounts which must appear in the statement. (Read ¶241) In the ledger purchases account is debited for total purchases, $3010.50; credited for *goods returned, $19.14;* for *rebates and allowances, $28.17;* total, $47.31; the difference ($3,010.50-$47.31) being the balance, $2963.19, shown in the trial balance.

In the ledger, sales account is credited for gross sales, $6824.50; debited for *goods returned, $12.30;* for *rebates and allowances, $56.91;* total, $69.21; the difference ($6824.50-$69.21) being the balance, $6755.29, shown in the trial balance.

The inventory at the close of the present fiscal period, December 31, is $5147.96.

From the figures shown in the trial balance, supplemented in the case of the purchase and sales accounts by those taken from the ledger, as given above, prepare a trading statement showing the gross trading profit. Then prepare two journal entries,—one which will open the trading account in the ledger (¶248), and one which will omit the trading account in the ledger (¶249), and present for approval.

Suggestion. The purpose of the closing journal entry may be further illustrated by opening a ledger account for each of the trading accounts named in the section of the trial balance shown in illustration 38 and then posting the amounts shown in the closing journal entry to these accounts, which will balance all of the ledger accounts excepting the inventory account, which will show the amount of the inventory at the close of the present fiscal period, and the profit and loss account which will show the gross trading profit.

(**2**) Harvey & Son's trial balance shows the following trading accounts at the semi-annual closing of their books, June 30, 19—. The inventory on that date was $29,336.45.

Prepare a trading statement showing the gross trading profit, with the proper journal entry to close when a trading account is opened in the ledger.

ILLUSTRATION 44.

Inventory - at close of last fiscal period			16000		
Purchases	Total purchases 45900. Goods rtd.	300.	45600		
Warehouse Supplies			475		
Warehouse Labor			850		
Sales	Total sales 38500. Goods rtd.	1500.			37000
Sales Discounts			490		

(**3**) The trading accounts shown in the trial balance of Hope & Hemphill, taken December 31, 19—, are as follows:

Prepare the trading statement and the journal entry to close, omitting the trading account in the ledger.

Note that separate accounts are kept for purchase and sales rebates and allowances, and that the balances shown by purchases and sales accounts, therefore, show total purchases and total sales. The inventory at the close of the present fiscal period is $8990.60.

ILLUSTRATION 45.

Inventory at close of last fiscal period	9455 28	
Purchases	22364 54	
Purchase Rebates & Allowances		148 50
Warehouse Supplies	370 20	
Warehouse Labor	1220	
Purchase Discounts		316 45
Sales		28343 77
Sales Rebates & Allowances	238 45	
Sales Discounts	432 50	

(4) The Chase Company's trial balance for the quarterly fiscal period ending September 30 showed the following accounts and balances:

Prepare a trading statement showing the gross trading profit for the period, and a journal entry to close the trading accounts without opening a trading account in the ledger. The inventory was $49312.30.

ILLUSTRATION 46.

Purchases	124365 90	
Sales		138984 12
Inventory	33400	
Freight In (189)	1743 45	
Warehouse Supplies	847 19	
Warehouse Labor	1463 70	
Purchase Rebates & Allowances		147 77
Sales Rebates & Allowances	438 68	
Purchase Discounts		454 86
Sales Discounts	711 28	

(5) In Peterson & Company's books, all items affecting the cost of purchases were entered directly into the purchases account. The various items charged and credited to that account were classified on an analysis sheet, with the following results:

Total purchases $66719.25; incoming freight, express and drayage charges, $793.50 (¶144*b*); duties, storage and other similar charges, $3670; purchasing agents' commissions and salaries, $1600 (¶144*c*); warehouse expenses, $2150. (¶191, ¶144*d*); purchases returned, $250 (¶145*c*); rebates and allowances on purchases, $378.50 (¶145*f*); goods shipped for sale on commission, at cost price, $1200 (¶145*h*); rebates allowed onincoming freight bills paid, $66 (¶145*f*). The inventory at the close of the last fiscal period was $9845; total sales, $59,718.50; discounts allowed on sales, $928.75. The inventory at the close of the present fiscal period is $26,750.

The following is the section of the trial balance showing these accounts as they appear in the ledger:

ILLUSTRATION 47.

Purchases	73038 25		
Inventory	9845		
Sales		59718 50	
Sales Discounts	928 75		

(*a*) Prepare the purchases account, showing the balance contained in the trial balance, indicating the various items in the explanation columns.

(*b*) Prepare a trading statement exhibiting in detail the above information shown by the accounts.

(*c*) Prepare a journal entry closing the trading accounts in the ledger without opening a trading account.

(*d*) What is the cost of the merchandise sold? What is the gross trading profit?

(*e*) If the present inventory were $23345.50, what effect would it have upon the result shown by the trading statement? (¶243)

(**6**) At the close of the first year of their business, the trading accounts in the books of Melton & Dane show the following results:

Total purchases, $41315; total sales, $39816; returned sales, $450; warehouse expenses, $475; warehouse labor, $950; sales discounts, $245. There was no inventory at the beginning of business. The present inventory is $7863.

(*a*) From this data, prepare the section of the trial balance showing the trading accounts.

(*b*) Prepare a trading statement showing the gross profit on sales.

(*c*) Prepare the journal entry to close the accounts without opening a trading account in the ledger.

ARITHMETICAL PROBLEMS—TRADING ACCOUNTS AND STATEMENTS.

(**1**) Inventory at the beginning of the fiscal period, $5350; total purchases, $9650; returned purchases, $214; incoming freight, $226; warehouse expense, $975. The present inventory is $4896; total sales, $13120; returned sales, $149. What is the net cost of purchases? (¶236) What is the cost of merchandise sold? (¶237, What are the net returns from sales? (¶238) What is the gross trading profit? (¶239)

Solution

Costs		Sales	
Invt	5350.	Total S.	13120.
Pchs	9650.	Ret S.	149.
Frt	226.	Net S.	12971.
W.Ex	975.	Net C.	11091.
	16201.	Gross P.	1880.
Ret C.	214.		
Net C.	15987.		
Invt	4896.		
	11091.	Cost of goods sold	

(**2**) Inventory at the beginning of the fiscal period, $6750; purchases, $27315, freight charges, $226; duties, $112; warehouse supplies, $133; warehouse labor;

$375; purchase rebates and allowances, $328.75; returned purchases, $95; purchase discounts, $212; total sales, $32421.50; sales discounts, $516; returned sales, $428.75. There is no inventory at the close of the fiscal period, as the goods were all sold.

What is the net cost of purchases? (¶236) What is the cost of the merchandise sold? (¶237) What are the net returns from sales? What is the gross trading profit or loss?

(3) Inventory account is debited for $8650. Purchases account is debited for $39,423.50; credited, $1126.12. Purchasing agent's commission and expenses, $628; warehouse expenses, $2065; duties, $845; merchandise shipped for sale on commission, at cost, $1600; purchase discounts, $894. Inventory at the close of the fiscal period, $7833.48; total sales, $43,318.60; sales discounts, $1225; returned sales, $983.

What was the net cost of purchases, cost of merchandise sold, the net returns from sales, and the gross trading profit or gross trading loss?

(4) Prepare arithmetical solutions of exercises 1, 2, 3, 4, 5 and 6 following ¶250, and present for approval.

PROFIT AND LOSS ACCOUNTS.

251. Profit and loss accounts are those accounts which show the *sources* of the various expenses and incomes of every description which result from conducting a business. They all have the effect of *increasing* or *diminishing* the capital of the concern.

252. Losses and gains come from three general sources:

(*a*) From the purchase and sale or the manufacture and sale of commodities, which are shown in the trading accounts.

(*b*) From the current expenses and incomes incidental to carrying on the business, which are shown in various accounts and groups of accounts in which are recorded the *cost* of and the *returns* from the *use* of property and things and the *services* of persons, such as selling expenses, administrative expenses, rent, interest, discount, commission, collection and exchange, and other similar accounts which may, therefore, be designated under the general name of *use and service accounts.*

(*c*) From special and extraordinary expenses and incomes, such as insurance, taxes, bad debts, repairs and renewals to buildings, rentals, purchase and sale of properties and all other similar items, depending upon the nature and extent of the business.

253. All profit and loss accounts show losses and gains *relatively*, because the costs of expenses or other losses shown in one account may be offset by the returns from incomes or other sources of gain shown in another account.

254. All the losses and gains of a concern could and may be entered directly into the profit and loss account, but in order to designate the *sources of the various expenses and incomes*, they should be classified either under separate accounts or on analysis sheets, so that they may be shown in the profit and loss statement in such detail as may be desired.

255. The principal sources of profit in an ordinary trading business are shown in the various trading accounts from which the trading statement, showing the gross trading profit, is prepared. This statement has already been described in ¶233 to 250 inclusive. In a manufacturing business a similar statement is prepared, which includes, however, various additional details shown by the manufacturing accounts.

256. The profit and loss statement shows the losses and gains from all sources, including the gross trading profit (or gross trading loss) shown by the trading statement, the object being to show the *net profit* or the *net loss* for the fiscal period included in the statement.

257. The sources of all expenses and incomes and of all losses and gains are of the utmost importance in economical and profitable business management. The principal purpose of modern accountancy is to supply such information to the business manager as will enable him to conduct a successful business, which means a *profitable* business.

258. It is for this reason that the services of the professional accountant have become so important in the organization of business concerns. He is expected to devise, install, and put into operation a system of accounts for any particular business that will give those *units of information* which will set forth accurately and in such detail as is necessary all the facts and results which will assist the management to administer its affairs intelligently.

259. It is from a comparison of the results shown for the different periods for which the business has been conducted that past mistakes in management may be avoided and new policies may be inaugurated.

260. The units of information which are necessary and useful, as well as the detail in which they are shown, vary greatly in different lines of business, depending upon its nature, its organization, and its extent. What might be an important item or unit of information in one business would be unimportant in another:

for instance, while a knowledge of the cost of each of the general expenses, such as fuel, light, office expenses, insurance, etc., might be necessary for the good management of one business, yet in another business these details would be unimportant. The same is also true of selling expenses, administration expenses, and all other sources of profit and of loss.

261. The student of accounts should endeavor to ascertain those units of information which are most important and useful in each line of business. This is fundamental to the organization of accounting systems. The object of this work is to train the student not only in the art of bookkeeping, but also in the organization of systems of accounting suitable for various lines of business, in so far as this is possible. (Read chapter on "Accountancy").

CURRENT EXPENSES AND INCOMES: USE AND SERVICE ACCOUNTS.

262. After goods are purchased and prepared for sale, when their cost ends (¶141) the selling expenses begin. Selling expenses consist of salesmen's salaries and commissions, salesmen's traveling expenses, the cost of samples and of sample cases, advertising in all its forms, delivery expenses, and all other expenditures incidental to selling the goods.

263. Salesmen's salaries and commissions and drivers' wages are paid for *services* rendered. Traveling expenses are paid for *services* rendered by railroads, hotels, etc. The outlays for sample cases, sample goods, premiums, etc., represent the cost of materials *used* in effecting sales. Advertising expenses are paid for *services* rendered by newspapers, magazines, and of printed matter and other materials *used* in effecting sales. Delivery charges represent the *use* of horses, wagons, and commercial motor vehicles in delivering goods, and the *services* of drivers, chauffeurs, etc.

SELLING EXPENSE ACCOUNTS.

264. All selling expenses may be entered in one account under an appropriate title, such as "Sales Expense" or "Selling Expense." When the various selling expenses are to be shown separately in the profit and loss statement, they may be classified to whatever extent desired by distributing them on an analysis sheet (¶490).

265. Separate accounts may be kept with any or all the various selling expenses, if it is so desired. It is usual to keep separate accounts with the more important items such as salesmen's salaries and commissions, traveling expenses, advertising, delivery expenses, freight out, etc.

Rule for Debiting and Crediting Selling Expense Accounts.

266. *Debit selling expense accounts for costs: credit for returns.*

266*a*. Debit **selling expense** accounts for the *cost* of uses, of services, and of materials employed in selling goods.

266*b*. Credit **selling expense** accounts for the *returns* from any uses, services, or materials previously charged to these accounts.

267. The various applications of the rule are as follows:

268. Debit selling expense accounts under appropriate titles,—

a. For *salesmen's salaries*.
b. For *salesmen's commissions*.
c. For salesmen's *traveling expenses*.
d. For cost of *sample cases, sample goods*, etc.
e. For cost of *premiums* given away to stimulate the sale of goods.
f. For the cost of all *advertising*.
g. For *delivery expenses* and charges, drivers' wages, etc., in retail and department stores, etc. (¶289)
h. For *branch office expenses*, mercantile references, etc.
i. For outward *freight*, express and drayage charges (¶278)
j. For *wrapping materials* such as paper, twine, etc., and for *wrappers' wages*.
k. For *storage* in outside warehouses, of goods ready for shipment.

269. Credit selling expense accounts under appropriate titles,—

1. For any returns for uses, services, and materials charged to these accounts or employed for other accounts, or for any overcharges or rebates on items charged to these accounts.

SUGGESTION.

Separate accounts may be kept for any one or more of the items indicated in the opposite column, depending upon the extent of the business and the number of items of the same kind which occur. When separate accounts are kept, they are treated in every respect exactly the same as you have been instructed for the sales expense account. Freight account ¶278 and delivery expense account ¶289 are examples of separate selling expense accounts.

270. **Observe** that in every instance selling expense accounts are debited for the *cost* of the uses, services and materials expended in selling goods.

271. **Observe** that in every instance selling expense accounts are credited for the *returns* from the cost of any use, service, or material charged to these accounts.

272. When separate accounts are kept for any one or more of the items enumerated in 268*a* to *k* inclusive, appropriate titles are indicated by the words in *italics*.

273. Transactions Illustrating the Various Applications of the Rule (¶266) for Debiting and Crediting Selling Expense Accounts.

Mr. Raymond's transactions affecting the sales expense account are as follows:

Jan. 3. He paid for sample cases, $22.35. (¶268*d*) – – Jan. 4. He paid for premiums, $27.65. (¶268*e*) – – Jan. 8. He paid for advertising, $39.

(¶268*f*) – – JAN. 31. He paid for delivery charges, $35. (¶268*g*) – – JAN. 31. He paid salesmen's salaries, $120 (¶268*a*); salesmen's commissions, $10 (¶268*b*); salesmen's traveling expenses, $30.90 (¶268*c*); for mercantile references, $6 (¶268*h*); for outward freight on goods sold f.o.b. delivery point, $12.50 (¶268*i*); for wrapping paper and twine, $8 (¶268*j*); for storage in an outside warehouse of goods ready for shipment, $6. (¶268*k*) Received cash for one small sample case, $2.20. (¶269*l*)

What was the cost of the various selling expenses for the month?

EXERCISE.

273*a*. Prepare a ledger account for the preceding transactions, as follows:

(**1**) Read and study each transaction carefully, referring to the special application of the rule for debiting and crediting purchases account indicated by the paragraph number.

(**2**) Apply the rule (¶266) and make the proper debit and credit entries in the sales expense account, indicating in the explanation column the nature of each item, as shown in the illustration. When completed, submit for approval.

ILLUSTRATION 49.

Sales Expense

19				19			
Jan.	3	Sample cases	22 35	Jan.	31	Sample case	2 20
	4	Premiums	27 65				
	8	Advertising	39				
	31	Delivery chgs.	35				
	31	Salesmens sales	120				
	31	Salesmens comm.	10				
	31	Traveling Expenses	30 90				
	31	Mer. references	6				
	31	Freight	12 50				
	31	Paper & twine	8				
	31	Storage 315.20	6				

273*b*. Illustration 49 shows the account as it appears January 31, when footed, preparatory to taking the trial balance.

273*c*. Illustration 50 shows the account as it appears after the profit and loss statement has been prepared and the journal entry, closing the profit and loss accounts, has been posted, at which time the accounts ruled and footed, as shown.

ILLUSTRATION 50.

4 Premiums	27 65	31 Profit & Loss a/c, to close	315 20
8 Advertising	39		
31 Delivery charges	35		
31 Salesmens sales	120		
31 Salesmens comn.	10		
31 Traveling Expenses	30 90		
31 Mer. references	6		
31 Freight	12 50		
31 Paper & twine	8		
31 Storage 315.20	6		
	317 40		317 40

TO CLOSE SELLING EXPENSE ACCOUNTS.

274. The object of these accounts is to show the net cost of the various expenses of the sales department and, incidentally, the amount that is to be deducted from the gross selling profit, as shown by the trading statement, in order to ascertain the *net selling profit*, as shown by the profit and loss statement.

275. The difference between the two sides of a sales expense account shows the *net cost* of making sales for the period, which is a *loss* that should be shown as a separate item (or items) in the profit and loss statement.

276. To close. After the profit and loss statement has been prepared, the sales expense accounts are closed by a journal entry made up from the profit and loss statement. When the closing item to each sales expense account has been posted, which should balance the account, rule the closing lines in red ink as shown in illustration 40, and enter the footings in black ink.

276*a*. Resource and liability inventories affecting these accounts are explained in ¶465.

EXERCISES IN SALES EXPENSE ACCOUNTS.

277. Prepare ledger accounts showing the account closed like illustration 50 for the following examples, applying the rule (¶266) for each transaction. Indicate briefly in the explanation column the nature of each item.

(**1**) DEC. 31. The sales expenses of the Richards Grocery Company, for the year are as follows:

Salesmen's salaries, $1500; salesmen's traveling expenses, $846.15; commission allowed to agents, $341.60; sample cases, $85; sample goods, $216.25; premiums,

$180.67; advertising circulars, $218.90; newspaper advertising, $116.45; postage for mailing advertising matter, $190; printing order books, $60; wages of drivers delivering goods, $480; horse feed, $126.50; horse shoeing, $23.25; delivery wagon repairs, $31.75; branch office salaries, $720; wrapping paper and twine, $65.30; wages of wrappers, $211.60; show-room rent, $60.

What is the net cost of the various expenses of the sales department for the year?

(**2**) The selling expenses for the Jones Mercantile Company for the half year ending June 30 are as follows:

Salesmen's salaries, $1200; traveling expenses, $618.26; sample cases, $45; sample goods, $185.30; premiums, $216.50; advertising, $175.16; order books, $25; wrapping paper, $45.60; delivery automobile supplies and repairs, $213.70; wages of chauffeurs, $600. The services of a salesman were used as a purchasing agent to the amount of $300. (¶269*l*)

What is the net cost of the sales expenses for the period?

Arithmetical Problems—Sales Expense Account.

(**1**) The Ritter Grocery Company's selling expenses for the quarter ending September 30 are as follows:

Salesmen's salaries, $900; salesmen's traveling expenses, $316.75; sample goods, $165; premiums, $137.50; printed matter for advertising, $111.60; postage $80; drivers' wages, $300; horse feed, $75; horse shoeing, $18; wagon repairs, $26.30. Sample goods were sold amounting to $57.50. The delivery wagon was used in hauling goods purchased to the amount of $78.75. Wrapping paper was used in re-casing goods purchased to the amount of $12.

What is the net cost of the selling expenses for the period?

(**2**) The Brown Shoe Company's sales expense accounts show the following footings for the fiscal year ending December 31:

Salesmen's commissions a/c, debit, $1567.18; credit, $9.60. Sample goods a/c, debit, $216.40; credit, $21.50. Advertising, debit, $262.81. Delivery expense a/c, debit, $387.90. "Freight out" a/c, debit $86.50; credit, $4.12.

What is the net cost of the selling expenses for the period?

OUTGOING FREIGHT EXPRESS DRAYAGE, ETC.

278. "Freight" or "freight out" is the heading used where a separate account is kept for freight charges on goods sold, which is a *selling expense.* (¶268*i*) It

includes all freight, express, drayage, cartage, and other charges incurred in the delivery of goods to the consignee by the consignor (i.e., the seller to the buyer) from the time the selling expenses begin, which in a wholesale or jobbing business is *from the time when the goods are made ready for delivery to the local customer, or on board cars for shipment,* or in a retail business *from the time the goods are ready for sale.*

279. The object is to show (1) the cost of freight, express and drayage charges paid on goods sold, (2) the amount (if any) of these charges rebated and returned (overcharges from mistakes in rating, etc.), and (3) from these to determine the amount to be deducted from the *gross profit on sales* to ascertain the *net profit on sales* in the profit and loss statement, which is shown by the *difference* between the two sides of "Freight Out" account, which should always show a debit balance.

280. This is the only separate freight account usually kept, as freight on purchases is properly chargeable to that account, therefore, "freight" account is generally understood by accountants to relate only to *freight outward.* This account can be omitted by debiting the items directly to sales expense account (¶268*i*)

Rule for Debiting and Crediting "Freight Out" Account.

281. *Debit for costs: credit for returns.*

The various applications are:

282. Debit **freight out** account,—

a. For all freight, express and drayage charges paid by us on outgoing goods.

b. For all freight, express and drayage bills paid by others for our account on outgoing goods.

283. Credit **freight out** account,—

c. For all rebates or other returns on charges previously debited to this account.

284. Observe that in every instance the account is debited for the *cost* of charges.

285. Observe that in every instance the account is credited for any *returns.*

286. The transactions for the items shown in the following account are not given, as they are all similar and easily distinguished from other selling expenses.

Illustration 51.

Freight

19 Jan. 5		32 30	19 Jan. 31	Profit & Loss to close	65 40
17		17 04			
28		16 06			
		65 40			65 40

287. The difference between the two sides of "Freight Out" account will show the cost of freight, etc., on goods sold, which is a *selling expense* that should appear as an item in the "sales expense" section of the profit and loss statement. (Illustration 87)

287*a*. Note that the difference between the two sides of a "Freight In" account will show a debit balance, which should appear as an item *increasing the cost of purchases* in the trading statement.

288. To close. After the profit and loss statement has been prepared, this account is closed by a journal entry which is made up from the entries appearing in the profit and loss statement. When the closing item for this account has been posted, which should balance it, then rule the closing lines in red ink and enter the footings in black ink.

288*a*. As this account is in every respect similar to the sales expense account, shown in illustrations 49 and 50, separate exercises are not deemed necessary.

288*b*. Resource and liability inventories affecting this account are explained in ¶465.

DELIVERY EXPENSE ACCOUNT.

289. Delivery expense account is a separate account for a class of items that, if preferred, may be charged directly to sales expense account. (¶268*g*) It is kept to show the cost of maintaining and operating the "delivery equipment," (¶428) such as costs of repairs and renewals of the equipment, feed supplies, drivers or chauffeurs' wages, gasoline and oil for automobiles, and all other items that enter into the cost of delivering goods.

290. The cost of delivering goods is a *selling expense* that should appear as an item in the "sales expense" section of the profit and loss statement, which is the reason for keeping a separate account for the items charged to it.

290*a*. Delivery expenses must not be confused with drayage charges. *Delivery expenses* include all charges on *outgoing goods* from the time the goods are ready for delivery to the local customer or on board cars for shipment, while *drayage charges* include all charges on *incoming goods* from depots and wharfs up to the time the goods are ready for sale, which should be included in the cost of purchases in the trading statement. (¶141, ¶144*b*, ¶146)

290*b*. When the same teams, automobiles, etc., are used for hauling the goods received as well as the goods delivered, delivery expense may be charged for the whole amount during the fiscal period. At the end of the fiscal period these expenses should be pro rated. A better method is to pro rate the expenses monthly, because the division would likely be more nearly correct when made monthly than when permitted to lie over until the end of the fiscal period.

Rule for Debiting and Crediting Delivery Expense Account.

291. *Debit delivery expense account for costs: credit for any returns from items charged to that account.*

292. The various applications of the rule are as follows:

293. Debit delivery expense account,—

a. For the cost of repairs and renewals of the delivery equipment.

b. For current supplies consumed, such as feed and bedding for horses, gasoline and oil for automobiles, etc.

c. For drivers' wages, bridge or ferry tolls, and for any other items that enter into the cost of delivering goods.

294. Credit delivery expense account,—

d. For any returns from the sale of items previously charged to this account.

e. For any returns or income for the use of the delivery equipment by others.

f. For the proportion of these expenses which should be charged to the purchases account for drayage on incoming goods.

295. The difference between the two sides of a delivery expense account shows the net cost of delivery expense for the period, which is a loss that should be shown in the sales expense section of the profit and loss statement.

296. To close. After the profit and loss statement has been prepared, in which the results shown by this account should appear as a separate item in the *sales expense* section, it is closed by a journal entry made up from the profit and loss statement. When the closing item to the account has been posted, which should balance the account, rule the closing lines in red ink and enter the footings in black ink.

296*a.* Resource and liability inventories affecting this account are explained in ¶465.

ADMINISTRATION EXPENSE ACCOUNT.

297. Administration expenses are the expenses incurred in the general management of a business considered as a whole, such as the salaries of officers and managers and of office help, the cost of office supplies, postage, stationery, traveling expenses, and such other miscellaneous expenditures as relate to the general management of the business.

297*a.* Salaries of officers and office help and traveling expenses represent the cost of *services* rendered. Postage represents the cost of a *service* rendered by the government. Office supplies, stationery, etc., represent the cost of materials *used.*

298. A single account under the head of "Administrative Expense" may be kept. If it is desired to show these expenses separately in the profit and loss statement, the items may be classified on an analysis sheet; or separate accounts with the various classes of items may be kept in the ledger, if preferred.

RULE FOR DEBITING AND CREDITING ADMINISTRATIVE EXPENSE ACCOUNTS.

299. *Debit administrative expense accounts for costs: credit for returns.*

300. The various applications of the rule are as follows:

301. Debit an administrative expense account, under an appropriate title,—

a. For officers and managers' salaries.
b. For salaries or wages of office help.
c. For office supplies, stationery, postage, telephone and telegram charges.
d. For traveling expenses of officers or employees of this department.
e. For any miscellaneous expenses of the administration, such as legal expenses, directors' fees, etc.

302. Credit the proper administrative expense account,—

f. For any returns from the services or materials charged to that account, or for any overcharges or rebates on items charged.

303. **Observe** that in every instance administrative expense accounts are debited for the *cost* of services and materials used in that department.

304. **Observe** that in every instance administrative expense accounts are credited for the *returns* from the cost of any use, service or material charged to them.

305. TRANSACTIONS ILLUSTRATING THE VARIOUS APPLICATIONS OF THE RULE (¶299) FOR DEBITING AND CREDITING ADMINISTRATIVE EXPENSE ACCOUNTS.

Transactions for January affecting administrative expense account are as follows:

JAN. 8. Paid for office supplies, $17.50. (¶301*c*) – – JAN. 12. Paid traveling expenses, $3.60. (¶301*d*) – – JAN. 16. Paid for legal advice, $10. (¶301*e*) – – JAN. 24. Paid for telegrams, $1.60. (¶301*c*) – – JAN. 31. Paid salaries of office help, $100. (¶301*b*) – – JAN. 31. Paid manager's salary, $150. (¶301*a*) – – JAN. 31. The services of one of the office clerks were loaned to the sales department to the amount of $7.70 (¶302*f*).

What was the cost of the administrative expenses for the month? (¶307)

EXERCISE

305*a*. Prepare a ledger account for the preceding transactions.

(1) Before entering each transaction, refer to the special application of the rule indicated in the paragraph number.

(2) Then make the proper debit and credit entries in the administrative expense account, applying the rule ¶299. When completed, submit for approval.

ILLUSTRATION 52.

Administrative Expense

19			19		
Jan. 8	Supplies	17 50	Jan. 31	Services	7 70
12	Traveling Expenses	3 60	31	Profit & Loss a/c. to close	275
16	Legal advice	10			
24	Telegrams	1 60			
31	Office help 275.	100			
31	Manager's Salary	150			
		282 70			282 70

TO CLOSE ADMINISTRATIVE EXPENSE ACCOUNTS.

306. The object of administrative expense accounts is to show the *net cost* of the various expenses of the administration department.

307. The difference between the two sides of an administrative expense account is the net cost of the administrative expenses for the period covered in the account, which is a *loss* that should appear as a separate item (or items) in the profit and loss statement.

308. To close. After the profit and loss statement has been prepared, administrative expense accounts are closed by a journal entry made up from the profit and loss statement. When the closing item to any administrative expense account has been posted, which should balance the account, rule the closing lines in red ink as shown in illustration 52 and enter the footings in black ink.

308*a*. Resource and liability inventories affecting these accounts are explained in ¶465.

EXERCISES IN ADMINISTRATIVE EXPENSE ACCOUNTS.

309. Prepare ledger accounts showing the accounts closed like illustration 50 for the following examples, applying the rule (¶299) for each transaction. No illustration is shown, as this account is in every way similar to the one shown in illustration 50. Indicate briefly in the explanation column the nature of each item.

(**1**) The Adams County Glass Company paid salary of manager, $3000; salary of bookkeeper and stenographer, $1200; stationery and office supplies, $157.16; postage, $122; telephone and telegrams, $71.65; directors' fees, $500; legal expenses, $200; extra office help, $150; traveling expenses of general officers, $346.18. They received a rebate on railroad ticket, $12.50. Received for use of our telephone for long distance calls by other people, $2.60.

What was the net cost of administrative expenses for the year?

(2) The Sun Mfg. Company's administrative expenses were as follows: Salaries of management, $5000; salaries of office help, $1800; stationery and office supplies, $142.75; postage, $130; telephone and telegrams, $81.50; legal expenses, $50; miscellaneous traveling expenses, $86.19.

What was the net cost?

ARITHMETICAL PROBLEMS—ADMINISTRATIVE EXPENSE ACCOUNTS.

(1) The Jones & Brown Mfg. Company's expenses for the year were:

Salary of manager, $4000; salaries of office help, $1600; stationery, $96.45; postage, $150; telegrams and telephone, $92.35; directors' fees, $700; legal expenses $380; traveling expenses, $167.18.

(2) The Midland Rolling Mill Company paid manager's salary, $2500; office help, $975; letter heads and envelopes, $60; postage, $72.30; telephone and telegrams, $61.25; directors' fees, $250; attorneys' fees for collecting accounts, $75; traveling, $30; banquet for officers, $75.

GENERAL EXPENSE ACCOUNTS.

310. An expense is the cost of any use or service from which no definite permanent value is derived; the cost of anything that is *used up* in conducting a business. General expenses consist of all expense items which are not included in the sales, administrative, manufacturing or other special expense accounts, such as the cost of rent, fuel, light, taxes, insurance, and miscellaneous items of similar character.

311. A single account under the head of "General Expense," or "Expense," may be kept, or separate accounts may be kept in the ledger with any one or more of the items, if desired. Insurance expense account ¶340 is an example of a separate general expense account. If a single account is kept and it is desired to show the items separately in the profit and loss statement, they may be classified on an analysis sheet.

311*a*. A single account for all expense items, including selling, administrative, manufacturing, and all other special and general expenses, may be kept under the heading, "Expense," if it is not convenient or desirable to keep separate accounts for the different classes of expense items. This is frequently advisable in small concerns. When the expense account is so kept, the items may be subdivided and classified to any extent desired, either monthly, quarterly, or annually, on analysis sheets (¶490), which permits of the various statements being prepared showing as much detail as if separate accounts were kept in the ledger for each class of expense items.

311*b*. It should be remembered that there is no other good reason for opening separate accounts for the different expense items than to show the cost of the various expenses separately in the trading and profit and loss statements. When detailed information regarding expenses is not necessary in the management of a business, it is a useless waste of time to classify expense items under many accounts. Where the volume of business is of considerable size, however, separate accounts should be kept with selling, administrative, and general expenses.

RULE FOR DEBITING AND CREDITING GENERAL EXPENSE ACCOUNTS.

312. *Debit general expense accounts for costs: credit for returns.*

313. The various applications of the rule are as follows:

314. Debit expense, under a general or special heading,—

a. For *rent, fuel and light, taxes, insurance* and other miscellaneous items of similar character.

315. Credit expense, under a general or special heading,—

b. For any returns from expense items charged to general expense accounts.

316. Observe that in every instance the account is debited for the *cost* of a use or service received.

317. Observe that in every instance the account is credited for the *returns* from a use or service previously charged to the account.

318. *Separate accounts* may be kept for any one or more of the items shown in *italics* in ¶314*a*.

319. TRANSACTIONS ILLUSTRATING THE VARIOUS APPLICATIONS OF THE RULE (¶312) FOR DEBITING AND CREDITING GENERAL EXPENSE ACCOUNTS.

The following are the general expenses paid for the month:

EXERCISE.

JAN. 10. Coal, $11.50. (¶314*a*) – – JAN. 14. Team License, $3.75. – – JAN. 18. Letter Box, $1.50.– – JAN. 31. Electric light, $3.81; rent, $90; rented space, sub-let, $25.00. (¶315*b*).

What are the total general expenses for the month? (¶322).

320. Prepare a ledger account for the preceding transaction like illustration 53, and present for approval.

ILLUSTRATION 53.

General Expense

19				19			
Jan.	10	Coal	11 50	Jan.	31	Rent	25
	14	Team licenses	3 75		31	Profit & Loss % to close	85 56
	18	Letter box	1 50				
	31	Elec. light	3 81				
	31	Rent	85 56				
			110 56				110 56

TO CLOSE GENERAL EXPENSE ACCOUNT.

321. The object of this account is to show the cost of the different general expenses incurred in conducting the business.

322. The difference between the two sides of a general expense account shows the net cost of the general expenses for the period, which is a loss that should appear as a separate item (or items) in the profit and loss statement.

323. To close. After the profit and loss statement has been prepared, general expense accounts are closed by a journal entry made up from the profit and loss statement. When the closing item to any general expense account has been posted, which should balance the account, rule the closing lines in red ink, as shown in illustration 53, and enter the footings in black ink.

323*a*. When insurance premiums are charged to general expense account for policies which do not expire within the fiscal period represented in the account, the premium value of the unexpired policy should be inventoried and general expense account should be credited for the amount. (Read "Resource Inventories," ¶468*a*) This method will have the result of placing the cost of insurance in the period to which it belongs. Another method of disposing of insurance, which is preferred by accountants, is given under the heading of "Insurance Account," ¶327.

323*b*. Resource and liability inventories affecting these accounts are explained in ¶465.

EXERCISES IN GENERAL EXPENSE ACCOUNTS.

324. Prepare ledger accounts for the following, showing the accounts closed like illustration 53, indicating briefly in the explanation column the nature of each item entered.

(1) The following are the expenses of Arthur Jones for January:

Rent, $100; coal, $17.50; gas, $30; electric light, $6.50; insurance premiums paid, $48; taxes, $75.84; city directory, $9; street car fares, $7.15.

(2) Charles F. Davison had the following expenses for February:

Rent, $125, coal, $5.60; gas, $45.60; electric light, $8.96; taxes, $100; rebate on gas bill $2.15; city directory, $8; car tickets, $5.

ARITHMETICAL PROBLEMS—GENERAL EXPENSE ACCOUNTS.

Charles A. Bell's expenses were as follows:

Rent, $125; coal, $26.50; gas, $27.50; taxes, $57.21; insurance premiums paid, $36; extra space rented, $25; directory, $8. What was the net cost of expenses for the period?

George Robinson had the following expenses:

Rent $200; gas, $113.75; electric light, $21.75; taxes, $98.43; cleaning windows $2.50; insurance, $75; desk space rented to others, $12; city directory, $5; meals for employees, $12. What was the net cost?

Edward Kelly paid during the month of April the following expenses.

Rent, $35; gas, $8.75; electric light, $4.50; taxes, $7.56; insurance premium, $12; rebate on insurance premium, $4; street improvement assessment, $14.87; city directory, $6. What were the total expenses?

INSURANCE ACCOUNT.

(*Unexpired Insurance Premiums*)

325. Insurance is a protection against loss which is guaranteed by insurance companies upon the payment of a premium based upon a percentage of the amount insured.

326. There are two methods of disposing of insurance transactions. One is to charge the premiums paid to the general expense account, as explained in ¶314*a*, ¶318 and ¶323*a*.

327. The preferred method generally followed by accountants, which is the method here explained, is to debit *insurance account* with the cost of all premiums paid on policies, whether fire, boiler, tornado, or indemnity, and to credit that account, at the end of each month, quarter or year, or at the end of a fiscal period, for the *premium value* of the insurance *which has expired or has been canceled,* the balance shown by the account being a *resource* (asset) equal to the value of the *unexpired premium value of the insurance policies in force.* When all policies have expired or have been canceled and have been credited, this account will balance.

328. The insurance which has expired under this method is debited to an *insurance expense* account, which is explained in the next chapter, ¶340.

329. The premium value of the insurance *which has expired* is found by dividing the premium on each policy in the proportion of the *expired* time (in months) to the *total* time covered in the policy. For instance, in a policy for one year, the premium on which is $75, the premium value which will expire for each month is one-twelfth of $75, or $6.25. If, when the books are closed at the end of a fiscal period, seven months of the twelve for which the policy is written have expired, the expired premium value of the policy would be $43.75, which should be charged to expired insurance account. This would leave an unexpired premium value on that policy of $31.25, which would be shown in the balance of the insurance account.

330. The purpose of crediting insurance account monthly or at the close of each fiscal period for the *expired premium value* of the policies is to have the cost of insurance for each month or fiscal period appear in the trial balance or the profit and loss statement covering the period for which the protection was received.

Rule for Debiting and Crediting Insurance Account.

331. *Debit insurance account for costs: credit for returns.*

332. The various applications of the rule are as follows:

333. Debit insurance account,—

a. For the cost of all premiums paid in advance.

334. Credit insurance account,—

b. For the proportion of the expired premium value of insurance which has expired or been canceled in the month or the fiscal period covered by the trial balance or by the profit and loss statement in which it is to appear.

c. For any rebates on premiums allowed or for any returns from open policies.

d. For allowances on premiums of canceled policies.

335. *When premiums are not paid* until the expiration of policies, i.e., *not paid in advance*, they should be charged directly to insurance expense account (¶341) or to the general expense account.

336. TRANSACTIONS ILLUSTRATING THE RULE (¶331) FOR DEBITING AND CREDITING INSURANCE ACCOUNT.

JAN. 1. Placed insurance in the American Insurance Company for $6000, policy No. 21316, at the rate of $1.50 per $100, for one year—insurance premium paid, $90. (¶333*a*) – – JAN. 31. The expired premium value of the above policy for one month is one-twelfth of $90, or $7.50. (334*b*)

What is the unexpired premium value of the policy Jan. 31, and the expired premium value? (¶337)

EXERCISE.

336*a*. Prepare a ledger account for the preceding transactions.

ILLUSTRATION 54.

Insurance

19				19			
Jan.	1	Premium	90	Jan.	31	Exp'd. pre. value	7 50
					31	Balance	82 50
			90				90
Feby.	1	Balance	82 50				

337. The difference shown by the insurance account is the *current premium value of the unexpired policies on hand* which should appear as a *resource* in the statement of resources and liabilities.

338. To close. An insurance account is not usually closed unless it is desired to show the value of the premiums on unexpired policies in one item, when the difference should be entered in red ink, or when it is necessary to forward the account to another page. To close the account, first find the difference, then enter on the credit side in red ink, (*a*) the amount of the difference, (*b*) the date, and (*c*) the word, "Balance." Then rule and foot the account, as shown in illustration 54, and bring down the balance on the *opposite side* (in black ink), entering the date of the next business day. If it is necessary to forward the account to another page, instead of bringing the balance down, forward it to the opposite side of a new

page, entering the number of the new page to which the account is transferred in the page column. In the new account in the page column enter the page from which the account was transferred. When all insurance policies have expired and have been charged off, this account will balance.

Exercises in Insurance Accounts.

339. Prepare ledger accounts for the following, showing the accounts closed like illustration 54, bringing down the balance on the opposite side of the account, as instructed in ¶338, and present for approval.

(**1**) Jennings Brothers placed the following insurance on their stock:

March 1, $8000, for one year at 1%, $80 (¶333*a*); Aug 1, $6000, for one year at 1¼%, $75; Nov. 1, $1000, for one year at 1¼% premium, $12.50. At the close of the fiscal year, December 31, the expired premium value on the policy of March 1, for ten months, at $6.66⅔ per month, is $66.67; on the policy of August 1, for five months, at $6.25 per month, $31.25; on the policy of November 1, for two months, at $1.04 per month, $2.08; total, $100. (¶334*b*)

What is the premium value of the unexpired policies on hand? (¶337)

(2) Harris Carter placed insurance on his stock as follows: January 2, $5000; March 15, $2000; April 1, $3000. Each policy is for one year, and the premium is at the rate of 96¢ per $100. July 1, he canceled the policy of January 2 for the unexpired time, receiving rebate, $20, being at the rate of 40¢ per $100 (¶334*b*, ¶334*d*).

What was the unexpired premium value of the policies in force at the end of the fiscal year, December 31, and what was the balance shown by the insurance account?

(**3**) Johnson & Davis placed insurance on their stock as follows:

Jan. 4, $4000; Feb. 28, $2000; March 25, $6000; July 7, $3000; Nov. 1, $2000; Nov. 1, $2000. Each policy is for one year from date, and the premium is at the rate of $1.08 per $100. They desire that the insurance account be credited monthly for the amount of the expired premium value on these policies.

What is the current premium value of the unexpired policies on hand Dec. 31?

Note: To find the exact expired premium value for less than a month, divide the amount for one month on the basis of thirty days. If exact value is not required, if less than one-half month, do not count; if one-half month or more, count as one month.

INSURANCE EXPENSE ACCOUNT.

(Expired Insurance Premiums.)

340. Insurance expense account is kept to show the amount of premiums which have expired during the month or other period represented in the account, which have, therefore, become an expense. The debit items to this account are *contra* to the credit items in the insurance account, i. e., this account is debited and insurance account is credited monthly, or for any other period, for the pro rata expired premium value of insurance policies. Insurance expense account is, therefore, in a sense, a companion account of the insurance account.

341. Insurance expense is also debited with all assessments on mutual policies for premiums that are not paid until the expiration of policies, such as "blanket" policies, etc.

Rule for Debiting and Crediting Insurance Expense Account.

342. *Debit insurance expense account for costs: credit for returns.*

343. The various applications of the rule are as follows:

344. Debit insurance expense, monthly or at the close of the fiscal period,—

a. For the expired premium value of insurance policies in force.

b. For premiums paid on mutual policies, or for premiums not paid until expiration of policies.

345. Credit insurance expense,—

c. For any returns from payments on expired premiums charged to this account.

346. Transactions Illustrating the Various Applications of the Rule (¶342) for Debiting and Crediting Insurance Expense Account.

Jan. 31. As shown in the second transaction, ¶336, the expired premium value of the policy referred to for one month is $7.50. (¶344*a*)

Illustration 56.

Policy No	Date	Name of Company	Property Insured	Amount	Time	Expires	Premium
16791	1911 Jan 5	Metropolitan	Stock	1000	1 yr.	Jan 5 '12	15
379642	Mar 15	Firemans	Furniture & Fixtures	500	1 yr.	Mar 15 '12	7 50
37042	July 16	Farmers	Stock	3000	1 yr	July 16 '12	45
761003	Sept 20	Germania	Building & Lot	6000	2 yr	Sept 20 '13	150

EXERCISE.

Prepare a ledger account showing the expired premium value of the policy for January, like illustration 55.

ILLUSTRATION 55.

Insurance Expense

19				19			
Jan. 31	Expired pre. value		7 50	Jan. 31	Profit & Loss A/c, to close		7 50

347. To close. Insurance expense account shows the *expired premium value* of the insurance policies in force for the period covered in the account, which is a *loss* that should appear as a separate item in the profit and loss statement. See illustrations 64 and 65. After the profit and loss statement has been prepared, this account is closed by a journal entry made up from that statement. When the closing item to the account has been posted, which should balance the account, if more than one item appears on either side of the account, rule the closing lines in red ink and enter the footings in black ink as shown in illustration 54. If but a single item appears on each side of the account, rule the closing lines as shown in illustration 55, as there are no footings to be entered.

348. This account may be omitted from the ledger by charging the items to the general expense account.

349. Prepare ledger accounts showing the expired premium value on policies named in transactions 1, 2, and 3, ¶339, and present for approval.

350. The following is a simple form of an insurance record book, showing the monthly expiration of premiums. By omitting the columns for each month, this book may be similarly used to show the expired premium value on insurance policies at the close of any fiscal year or period.

	Expirations												Amount Carried Forward
Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	
1 25	1 25	1 25	1 25	1 25	1 25	1 25	1 25	1 25	1 25	1 25	1 25	
		31	62	63	62	63	62	63	62	63	62	5 93
						187	3 75	3 75	3 75	3 75	3 75	20 62
								208	6 25	6 25	6 25	20 83

INTEREST AND DISCOUNT.

351. The use of money is interest. When the use of money is paid for *after* the use is received, it is called *interest*; when the use is paid for *before*, it is received it is called *discount*. Discount is interest *paid in advance*. This is really the only difference in the terms and for that reason a single account under the title of "Interest" is usually kept for both interest and discount. Separate accounts may be kept with "Interest" and with "Discount," or they may be combined under the head of "Interest & Discount," or the interest derived from a particular source may be kept in a separate account, as "Interest on Borrowed Capital," or "Interest on Loans."

351*a*. *Illustration*. If A borrows \$100 from B for one year at 6% interest, at the expiration of that time (*after* he has received the use or interest) he will return \$100 to B plus \$6, or \$106. The \$100 is in payment of the loan. The \$6 is in payment for the use (interest) of \$100 for one year. If the \$6 is deducted from the \$100 when the loan is made, it is then called *discount*, because it is paid in advance, or *before* the borrower has had the use of the money.

352. In a bookkeeping sense interest is understood to refer to money borrowed to increase the capital of the business or to money loaned from the surplus funds of the business. Interest on loans should be distinguished from discounts on purchases and sales. (¶214)

352*a*. *Interest on partners' capital* is not, strictly speaking, an expense of conducting the business and therefore should not be debited to interest account. Instead it is generally treated as a direct charge to profit and loss account. Interest on partners' capital may be eliminated entirely from both the interest and the profit and loss accounts by considering the total interest due the partners as a liability of the firm, debiting each partner for his share and crediting each partner for the interest owed to him.

353. Interest is calculated on interest bearing notes from the date on which they begin to draw interest to the date they are due. Discount is calculated for the exact number of days from the date of discount to the date due. Interest bearing notes are discounted for the *amount* of the note, which is the *face* of the note *plus* the *interest*. The amount of the note less the discount equals the *proceeds*. On open accounts interest is calculated from the date on which the account (or items) is due until the date on which it is paid.

354. A clear understanding of interest will be had in connection with any transaction if the student will ask the question, "Do we *receive the use* of money borrowed or loaned, or do we *give the use* of it?" If we *receive* the use, it is a *debit* to interest account (¶28); if we give the use, it is a *credit* (¶29).

355. The use received or given must not be confused with the money received or paid. It is the *use* that is received or given, and the use is paid for in cash or otherwise like any other commodity.

Rule for Debiting and Crediting Interest Accounts.

356. *Debit interest accounts for costs: credit for returns.*

356*a*. Debit interest accounts for the *cost* of the use of money received.

356*b*. Credit interest accounts for the *returns* from the use of money given.

357. The various applications of the rule are as follows:

358. Debit interest, under the proper title,—

a. For all interest accrued and owing to us from others on notes receivable, *bonds, accounts, or other claims at the beginning of business, which will be credited to this account when received.

b. For the use of money (interest) received by us on our notes (notes pay.), accounts etc., and for which we pay or allow credit.

c. For the use of money (discount) received by us on notes and time drafts that are discounted for us by others.

d. For the use of money (discount) received by us, when others prepay their own notes or acceptances (notes rec.) in our favor.

e. For the use of money received by us (discount) on notes and drafts we transfer to others before maturity, for purchases or on account.

f. For accrued interest owing *to others* at the close of the fiscal period, as shown by the inventory of *accrued interest payable* (¶468*b*).

g. For accrued interest owing *to us at the close of the last preceding fiscal period,* as shown by the inventory of *accrued interest receivable.*

359. Credit Interest, under the proper title,—

h. For all interest accrued and owing to others on notes payable, *bonds accounts, etc., at the beginning of business, which will be debited to this account when paid.

i. For the use of money (interest) given to others on their notes (notes rec.) accounts, etc., and for which they pay or give us credit.

j. For the use of money (discount) given to others on their notes and acceptances that are discounted for them by us.

k. For the use of money (discount) given to others, when we prepay our own notes (notes pay.) in their favor.

l. For the use of money (discount) given to others on notes and drafts they transfer to us before maturity for purchases or on account.

m. For accrued interest owing *to us* at the close of the fiscal period, as shown by the inventory of *accrued interest receivable* (¶468*a*).

n. For accrued interest owing *to others at the close of the last preceding fiscal period,* as shown by the inventory of *accrued interest payable.*

*Interest on bonds is generally recorded in a separate account, because it is always shown separately in the profit and loss statement. Interest on bonds should always be accrued monthly.

360. Observe that in every instance the account is debited for the *cost* of the *use of money* received.

361. Observe that in every instance the account is credited for the *returns* from the *use of money* given.

362. TRANSACTIONS ILLUSTRATING THE VARIOUS APPLICATIONS OF THE RULE (¶356) FOR DEBITING AND CREDITING INTEREST ACCOUNTS.

Transactions for January affecting interest account are as follows:

JAN. 1. Interest accrued and owing to us from others at the beginning of business, $9.17. (¶358*a*) – – JAN. 1. Interest accrued and owing to others at the beginning of business, $3.47. (¶359*h*) – – JAN. 5. Paid for interest on a note maturing today, $3.65. (¶358*b*) – – JAN. 7. Our note was discounted at bank at 30 days, amount of discount, $2.50. (¶358*c*) – – JAN. 9. Received payment for note in our favor, and also the interest amounting to $4.12. (¶359*i*) – – JAN. 10. A customer prepaid his note in our favor less discount to maturity, amount of discount, $1.17. (¶358*d*) – – JAN. 12. As an accommodation we discounted a friend's note for $250 at 30 days, amount of discount being $1.25. (¶359*j*) – – JAN. 14. We prepaid our note in favor of B. A. Watson less discount to maturity, amount of discount, $3.27. (¶359*k*) – – JAN. 15. Hamilton & Company have transferred to us, on account, a note in their favor less discount to maturity, discount $5.66. (¶359*l*) – – JAN. 17. We transferred to Mitchell Sons, on account, note in our favor less discount to maturity, the discount being $1.12. (¶358*e*) – – JAN. 31. An inventory of the interest which has accrued on our interest bearing notes in favor of others shows that we owe accrued interest payable, $12.44. (¶358*f*) – – JAN. 31. An inventory of the accrued interest owing to us on notes in our favor shows that others owe us accrued interest receivable amounting to $7.66. (¶359*m*) – – JAN. 31. The accrued interest owing to us at the close of the last preceding fiscal period for which this account was then credited was $8.94. (¶358*g*) – – JAN. 31. The accrued interest owing to others at the close of the last preceding fiscal period for which this account was debited was $6.56. (¶359*n*)

What is the gain or loss from interest for January? (¶364)

EXERCISE

363. Prepare a ledger account for the preceding transactions like illustration 57, and present for approval.

ILLUSTRATION 57.

Interest

19			19		
Jan. 1		9.17	Jan. 1		3.47
5		3.65	9		4.12
7		2.50	12		1.25
10		1.17	14		3.27
17		1.12	15		5.66
31		12.44	31		7.66
31	7.00	8.94	31		6.56
			31	Profit & Loss ✓ to close	7
		38.99			38.99

To Close Interest and Discount Accounts.

364. The difference between the two sides of an interest or a discount account shows the loss or gain—a *loss* when the *debit* side is the larger, a *gain* when the *credit* side is the larger. In either case it should appear as a separate item in the profit and loss statement. (Illustration 87)

365. To close—After the profit and loss statement has been prepared, interest and discount accounts are closed by a journal entry made up from the profit and loss statement. When the closing item to any interest or discount account has been posted, which should balance the account, rule the closing lines in red ink, as shown in illustration 57, and enter the footings in black ink.

365*a*. The method of disposing of inventories for *accrued interest receivable* and *accrued interest payable* is explained in ¶468.

Exercises in Interest and Discount Accounts.

366. Prepare ledger accounts for the following transactions, showing the accounts closed like illustration 56, applying the rule (¶356) for each transaction.

(**1**) Oct. 1. Paid for interest on our note due today at bank, $7.45. (¶358*b*) – – Oct. 5. The bank discounted for us J. M. Robinson's acceptance in our favor, discount for 30 days, $4.58. (¶358*c*) – – Oct. 8. Samuel Walker paid his note in our favor with interest due today; the interest was $7.50. (¶359*i*) – – Oct. 12. Frank Brown paid his overdue account including interest; interest for three months, $8.25. (¶359*i*) – – Oct. 15. William Franklin transferred to us J. N. Scott's 30-day note less a discount of $2.54. (¶359*l*)

What does the difference of the account show—a loss or a gain and how much?

(**2**) William Bond's transactions affecting interest and discount account for the month of April are as follows:

April 2. He paid interest on an overdue account in favor of Johnson & Son, $3.47. – – April 5. James Richard prepaid his note in Bond's favor by agreement; the discount was $2.50. – – April 9. He transferred J. N. Brown's note in his favor to William Walker on account, less discount, $1.56. – – April 16. He received interest on William Brown's overdue account, $2.45. – – April 23. He paid his note in favor of R. N. Bates, less a discount of $2.50. (¶359*k*) – – April 30. He owed interest to others, which has accrued to date, on notes and open accounts, $12.45. (¶358*f*).

What is the result shown by his interest and discount account?

(3) E. D. Vane & Company's transactions affecting interest and discount account for the year are as follows:

JAN. 1. The accrued interest owing to them at the close of the last preceding fiscal period (December 31), as shown by the inventory of accrued interest receivable, was $215.12. (¶358*g*) – – They owed interest to others at the close of the last fiscal period (December 31), as shown by the inventory of accrued interest payable, $14.65. (¶358*n*) – – FEB. 5. They paid for the use of money borrowed on their notes, $341.90. (¶358*b*) – – MARCH 31. They gave the use of money to their various customers on their notes and acceptances which they discounted, to the value of $74.12. (¶359*j*) – – APRIL 30. The discount on notes and drafts which they transferred to others before maturity amounted to $18.25. (¶358*e*) – – MAY 31. During the month they discounted for others various notes and acceptances, the discount on which amounted to $47.76. (¶359*j*) – – JUNE 30. They prepaid during the month three of their own notes, thereby saving a discount of $67.77. (¶359*k*) – – JULY 31. During the month two customers prepaid their notes, less discount to maturity; the amount of the discount was $18.50. (¶358*d*) – – AUG. 31. During the month they had various notes, acceptances and time drafts discounted at bank, the discounts amounting to $33.71. (¶358*c*) – – SEPT. 30. The notes and acceptances of various customers were transferred to them before maturity for purchases and to apply on account; the discounts amounted to $84.76. (¶359*l*) – – DEC. 31. At the close of the year they find they owe on accrued interest payable, $345.75 (¶358*f*) and that others owe them on accrued interest receivable, $427.27 (¶359*m*).

What result is shown by the interest and discount account at the closing of the books?

ARITHMETICAL PROBLEMS—INTEREST ACCOUNTS.

During the month of November, C. F. Scharfe received and paid interest as follows:

Interest on his notes receivable paid in cash, $25.75; discount on notes and acceptances discounted for others, $97.42; discount on his notes that were discounted for him by others, $3.50; interest received on money loaned to others, $84.50.

What were his net returns from interest?

PROPERTY INVESTMENT EXPENSE AND INCOME ACCOUNTS.

367. In connection with almost every business there is an investment of some part of the capital in various forms of property, such as real estate, furniture, fixtures, horses, wagons, harness, machinery, tools, patterns, patent rights, etc., that

are not included in and form no part of the special line of goods bought, sold or manufactured, but which are necessary in carrying on the business. The accounts showing these investments are known as *capital investment* accounts. They show the amount of the capital of the concern invested in various kinds of property that is not immediately available for the payment of current debts or expenses.

368. Capital investment accounts should show only the *cost value* of the property represented in the account. Whenever anything is sold that has been charged to an investment account, an entry should be made which will credit the account for *the original cost price of what is sold,* the object being to have the account show at all times *the original cost price of the property on hand.* If the selling price is greater than the original cost, the difference or gain should be credited directly to profit and loss account or it may be credited to a special account under a title that will indicate the source of the income. If the selling price is less than the original cost price, the difference should be debited to profit and loss account, unless a depreciation or other reserve fund has been set apart to meet the loss, when the account for that fund should be debited. Losses and gains from capital investment accounts should appear as separate items in the profit and loss statement.

369. In addition to the investment in properties shown by the investment accounts, various expenses are incurred in their maintenance and from many of them an income is returned; consequently a separate *expense and income* account should be kept with each investment, to show the cost of maintenance, expenses, etc., on one side and the income or returns from the investment on the other.

370. Expense and income accounts relating to investments should show only the *gain or loss arising from the current use or employment* of the property. Any gain or loss arising from an increase or decrease in the value of the property affects the investment account and should be disposed of as described in ¶368.

371. Observe, therefore, that there are generally *two accounts* opened in connection with the ownership of property—one showing the *investment* in the property and the other showing the expenses of the property and the income from the property and, consequently, the *gain or loss resulting from the investment.*

372. It is sometimes difficult to determine whether items representing outlays affecting these accounts should be charged to the investment or to the expense and income account. The following are the rules usually observed by accountants:

(*a*) All expenditures made on the property, whether for first cost or for improvements, *up to the time the property is ready for use or becomes productive* should be charged to the *investment* account.

(*b*) All sums expended on the property *which increase the selling or rental value* of the property should be charged to the *investment* account.

(*c*) All sums expended to maintain the property at its present cost, selling or rental value should be charged to the *expense and income* account.

373. As the method is the same for keeping the various investment expense and income accounts, only those for real estate will be explained and illustrated in detail. Briefer explanations of other similar accounts will follow.

REAL ESTATE.

374. This is a general name that is applied to what is known as *real property* which consists of land, houses, etc. Accounts with each property should be kept under appropriate headings, as "House and lot, 96 North St.," or "18th Street Store Property," or "Elm Township Farm," with separate accounts for the *investment* and for the *expenses* and *incomes*.

375. Not infrequently there is a considerable variation in the increase or decrease of the value of land and the buildings thereon. Usually there is a gradual depreciation in buildings while there is a gradual increase in the value of land. The decrease in the value of the buildings should be taken account of annually, which would directly affect the current gains and losses of the business for the period, while the increase in the value of the land is seldom considered until the land is finally disposed of. For these reasons it is not unusual that two accounts are kept—one with the land, under the title of "Real Estate," and the other with the structures or other property thereon, under the title of "Buildings."

THE INVESTMENT ACCOUNT—REAL ESTATE

A capital Investment Account Showing a Resource.

376. Real estate investment accounts should be opened under appropriate headings followed by the word "Investment," as, "Real Estate Investment," or where separate accounts with each property are kept, "House and Lot 96 North St.,—Investment." Such accounts are purely resource (asset) accounts.

377. *The object* is to show the cost of the investment, which includes (*a*) the first cost of the land or property purchased including the buildings or other improvements thereon, also the cost of surveying, examination of title, recording fees, commissions etc., (*b*) cost of all permanent improvements which result in *increasing the earning or rental value* of the property, such as repairs, grading, side-walks, sewers, etc. and (*c*) cost of taxes, interest on mortages, or other items of cost *up to the time the property becomes productive or is ready for use.*

RULE FOR DEBITING AND CREDITING REAL ESTATE INVESTMENT ACCOUNTS.

378. *Debit real estate investment accounts for costs: credit for returns.*

378*a*. Debit real estate investment accounts for *costs*.

378*b*. Credit real estate investment accounts at the cost price of the property sold or otherwise disposed of. (Read note.)

379. The various applications of the rule are as follows:

380. Debit the investment account, under its appropriate title,—

a. For the cost or appraised value of the property on hand at the beginning of business.

b. For all purchases of property, and for all additional costs to the property and improvements *until it is ready for use or occupancy or becomes productive.*

c. For all permanent improvements made thereafter that will *increase the permanent value* of the property or the *rental or other income from the investment.*

d.* For commissions on purchases of the property.

381. Credit the investment account, under its appropriate title,—

e. For all sales of the property at its *cost* value, i. e., for the *original price charged to the account.*

NOTE: The *returns* or incomes from the property are shown in the expense and income account.

**Commission on sales* represents the cost of a particular service rendered for which it is the best practice to keep a separate commission account to which all such items should be debited.

382. **Observe** that in every instance the account is debited for the *cost* of the property represented by the total investment.

383. **Observe** that in every instance the account is credited for the *original cost price* of the property disposed of.

384. TRANSACTIONS ILLUSTRATING THE VARIOUS APPLICATIONS OF THE RULE (¶378) FOR DEBITING AND CREDITING REAL ESTATE INVESTMENT ACCOUNTS.

(1) Illustrating the transactions and the account for property purchased to be used in connection with the business, i. e., in which the business is located.

JAN. 1. Purchased property located at No. 9 W. Main St., consisting of a store building and two lots, $11,500. (¶380*b*) – – JAN. 5. Paid for permanent improvements on the property by enlarging rear entrance and building shipping platform, $450. (¶380*c*) – – JAN. 6. Paid for surveying, examination of title, and recording deed, etc., $63.75. (¶377*a*, 380*b*) – – JAN. 12. Paid purchasing agent's commission (¾%) $86.25. (¶380*d*) – – JAN. 25. Sold unoccupied lot adjoining the lot on which the building is situated for $3600, the cost value of which was $3000, the profit, $600, being retained by the proprietor. (¶381*e*)

What is the cost value of the property on hand at the close of the fiscal period, January 31? (¶385)

Prepare a ledger account like the following illustration.

ILLUSTRATION 58

Real Estate #9 W. Main St.

19					19		
Jan.	1		11500		Jan.	25	3000
	5		450			31 Balance	9100
	6		63 75				
	12	9100.	86 25				
			12100				12100
Feby.	1	Balance	9100				

TO CLOSE REAL ESTATE INVESTMENT ACCOUNTS.

385. The difference between the two sides of a real estate investment account shows the *original cost value of the property* on hand, which is a *resource* (asset) that should appear as an item in the statement of resources and liabilities. (Illustration 93.)

386. To close. A real estate investment account is not usually closed unless it is desired to show the value of the investment in one item or to forward the account to another page, when the difference should be entered as a balance on the credit side of the account in red ink, after which the account should be ruled in red ink and footed in black ink, when the balance should be brought down on the opposite side in black ink as shown in illustration 58 or forwarded to the opposite side of the account on a new page. When the property represented in the account is finally disposed of, the account will balance.

REAL ESTATE EXPENSE AND INCOME ACCOUNTS.

387. Real Estate Expense and Income, is an appropriate heading when a single account is kept for one or more properties. If separate accounts are kept with each property, they may be designated by the location of the property, such as "Real Estate, 96 North St.—Expense and Income," or "House and Lot, 26 Elm St.–Expense and Income." Separate accounts with expenses and with incomes may be kept if desired. In many instances this plan is preferable. A real estate expense and income account is a purely profit and loss account and in no way affects the results shown by the investment account.

388. The object is to show the current expenses of the property *after it has been prepared for occupancy or use,* such as expenditures for preservation, taxes, insurance, repairs, commissions for renting, interest on mortgages, light, heat, janitor service, depreciation, etc., on the one side, and the gross income from rentals or other sources on the other side, and from these to ascertain *the amount gained or lost* on the investment. It is from this account that the owner is enabled to calculate the percentage of profit (or loss) on the investment.

Rule for Debiting and Crediting Real Estate Expense and Income Accounts.

389. *Debit real estate expense and income accounts for costs: credit for returns.*

390. The various applications of the rule are as follows:

391. Debit the expense and income account under its appropriate title.—

a. For the cost of repairs, preservation, or other improvements to maintain the property in good condition *when such improvements do not increase its rental value.*

b. For taxes, insurance, interest, and other similar charges on the property for the fiscal period.

c. For the cost of light, heat, janitor service, etc., when payment for the same is included in the income from rentals.

d. For agents' commissions for renting, collecting rent, etc.

392. Credit the expense and income account under its appropriate title,—

e. For all returns in the way of rents, sales of products or other incomes from the property.

f. In the case of farms or other property operated by the owner, for the sale of all products, and for the value of all products taken for private use at market price.

Note: Property used by the owner as a residence or place of business is seldom credited for any income value, although when used as a place of business, it is not unusual to consider its rental value as an income which, when credited, should be debited to the proper expense account.

393. **Observe** that in every instance the account is debited for the *cost* of some outlay which is an expense to the property.

394. **Observe** that in every instance the account is credited for the *returns* from some income from the property.

395. Transactions Illustrating the Various Applications of the Rule (¶389) for Debiting and Crediting Real Estate Expense and Income Accounts.

(1) Example illustrating the transactions and the account for property in which the business of the owner is conducted.

Jan. 16. Paid for repairs to the roof, $16.50. – – Jan. 25. Paid for replacing broken glass in windows, $2.56. – – Jan. 31. The monthly proportion of taxes paid is $3.50; the monthly proportion of insurance is $8.50.

What is the net cost of the expenses on real estate for the month?

Prepare a ledger account like the following illustration.

ILLUSTRATION 59.

Real Estate, Expense & Income

19			19		
Jan. 15	Repairs	16 50	Jan. 31	Profit & Loss A/c to close	31 06
25	"	2 56			
31	Taxes	3 50			
31	Insurance	8 50			
		31 06			31 06

TO CLOSE REAL ESTATE EXPENSE AND INCOME ACCOUNTS.

396. The total footing of the debit side of a real estate expense and income account shows the *total expense* of the property for the period; the total credit footing shows the *total income* from the property for the period. *The difference* between the two sides of the account shows the *net gain* or the *net loss* on the investment—a loss when the debit side is the larger, a gain when the credit side is the larger,—which should appear as a separate item in the profit and loss statement. When it is desired to show the total expenses and the total income, the footings may be inserted to the left of the amount columns in the profit and loss statement, extending the difference into the proper column.

397. To close. After the profit and loss statement has been prepared, real estate and income accounts are closed by a journal entry made up from the profit and loss statement. When the closing item has been posted, which should balance the account, rule the closing lines in red ink as shown in illustration 59, and enter the footings in black ink.

397*a*. Resource and liability inventories affecting this account are explained in ¶468.

398. Illustrating the rules under ¶378 and ¶389, if the improvements mentioned in ¶380*b* *do not increase the earning or rental value* of the property, their cost should be charged to the *expense* account; and likewise if the items mentioned in ¶380*c* *do not increase the rental value*, they should be charged to the *expense* account if they are created *after the property becomes productive or is ready for use.*

399. Where an improvement does not increase the rental value or income but does increase the *permanent* or *selling* value of the property it is the rule to charge the cost to the *investment* account, but a sharp distinction must be made between what constitutes a *material* increase in the permanent or selling value and that which is merely an expense.

400. A single real estate expense and income account may be kept to include the expenses of and returns from a number of properties when it is not deemed neces-

sary to keep a separate expense and income account for each property. Such an account would show the total expenses of all the real estate included and the total income from the same, the difference being the *net profit* or the *net loss* on the investments for the period covered in the account.

401. When such an account is kept, the expenses and incomes relating to each property included may be separated on an analysis sheet at the end of the fiscal period. This method has the advantage of reducing the number of accounts in the ledger.

402. EXERCISES IN REAL ESTATE INVESTMENT, EXPENSE AND INCOME ACCOUNTS.

The following transactions involve both investment and expense and income accounts. Prepare ledger specifications for each, applying the rules (¶378, ¶389) in determining the proper debits and credits. When completed, present for approval.

(**1**) APRIL 5. Frank P. Kennedy purchased a lot on the corner of High and Chestnut Sts. for $1000. (¶380*b*) – – JUNE 30. Paid for surveying, $7.50 (¶377*a*); recording deed, $1.50; excavating foundation for building, $175; contract for material and labor for brick work, $3216.94; material and labor of carpenters, $1875.62; tiled floors, $750; plumbing, $397.15; roofing, $307.80; grading yard, $65; cementing cellar, $54.50; constructing sidewalks, $87.60; preparing lawn and sowing grass seed, $6. – – APRIL 12. He received for the sale of old building on lot at time of purchase, $65 (¶381*e*). The building was ready for occupancy July 1. During the first year he received rental, $2000, (¶392*e*) entered under date of June 30. His expenses were: MAR. 5, taxes, $187.60; (¶391*b*) – – APRIL 1, insurance, $150; MAY 15, water rent, $60; sundry repairs on building, $18.36; assessment for street cleaning, $18.54; JUNE 30, upkeep of lawn, $30; electric lighting, $120; (¶391*c*) coal and gas, $237.50.

What was the cost value of the property on hand (¶385) and what was the net income from the property for the year ending June 30? (¶396)

(**2**) JAN. 1. John F. Richards purchased the Mann building for $15,000, giving in payment cash, $10,000, and a mortgage for $5000, bearing interest at 6%. – – FEB. 1. Received cash for rent, $300. – – FEB. 5. Paid for insurance (1 year) $160. – – MARCH 1. Received rent, $320. – MARCH 2. Paid janitor's salary for January and February, $75. – – MARCH 4. Assessment for grading and curbing, $42.13. – – MARCH 8. Paid carpenter for changing partition, $20, for which the tenant agrees to pay $5 more rent per month. (¶380*c*) – – MARCH 15. Water rent (3 months) $35. – – MARCH 20. Putting new locks, keys, etc., on doors, $8.75. – – MARCH 31. Rental for March, $350; elevator repairs, $85.20; janitor's salary for March, $37.50; electric light bill for 3 months, per contract, $30; new letters for directory, $3.50; asbestolith flooring for halls, $216.30.

Show the investment and the expense and income accounts for the quarter ending March 31.

ARITHMETICAL PROBLEMS—REAL ESTATE ACCOUNTS.

(1) JAN. 1. The West Side Stock Yards Company began the construction of their new yards. The different construction charges were as follows: grading yard, $476.18; iron pipe, brick work, miscellaneous material for underground construction, $2617.80; lumber and labor for overhead construction, $3291.70; office building, per contract, $1697.30; fixtures in office building, $275; plumbing in office building, $36.40; insurance premiums expired during construction, $76.50: rent of ground from B. & O. Railroad during construction, $275; interest on bank loan during construction, $60; office expenses—telephone, telegrams, stationery, postage, etc., during construction, $86.45. – – FEB. 1. The building and yards were rented to the West Side Commission Company, and the construction company's expenses were as follows: feed purchased, $187.30; repairing broken gates, $86.45; lumber and material for building additional yards, $376.18; plumbing for additional yards, $127.30; new insurance taken, $36; taxes, $54.35. They received for feed sold, $153.19; for rent, $460; for insurance, $49.60; and other miscellaneous income, $126.37.

What was the cost of the stock yard; also the total expense, the total income and the net gain or loss?

(2) JULY 1. The buildings, land and all improvements of the Granville Glass Company were purchased at receivers' sale for $6500. The necessary expenditures by the purchaser in order to put the plant in running condition were as follows: fire brick, $1487.96; tank blocks, $986.14; lumber, $784.32; miscellaneous hardware and other material, $396.45; labor during construction, $2165.70; superintendence, $600; gas and other fuel used during reconstruction period, $1100; iron pipe, $270. – – SEPT. 1. The plant started to make glass at its full capacity. – – Other charges since Sept. 1 have been, for miscellaneous hardware, $143.16; repairing roof of building, $28.16; blacksmith shop expenses (repairing tools, etc.), $295.60; tank blocks, $487.16; fire brick, $232.12; replacing old cutters' tables, $300; sold old tables for $60.

What is the total cost of the plant and of maintenance?

403. The real estate investment, expense and income accounts described in the preceding pages, beginning with ¶387, represent these accounts as they are kept in the books of the owner, and must not be confused with the accounts that would be kept by a real estate agent, although the principles involved are quite similar. The real estate accounts of agents, trustees, administrators, etc., will be fully explained in a later chapter.

FURNITURE AND FIXTURES.

404. Under this heading is kept an account with *furniture*, such as desks, tables, chairs, or other articles that may be used in the furnishing of a store, dwelling, factory, or any place of residence or business, and with *fixtures*, which include such articles as gas fixtures, shelving, counters, show cases, electric fans, filing cases, typewriters, office safes, etc.

405. Two accounts are usually kept—one showing the capital investment, and the other showing the cost of repairs and renewals.

406. The investment account is kept for the purpose of showing the original cost of the furniture and fixtures. The original cost is neither increased nor decreased while the articles remain in use, so that in case of fire or for any other reason the books will show the *original cost of whatever was destroyed.* When anything charged to this account is disposed of the account is credited, not for the selling price but for the *original cost price* debited to the account. The account will therefore always show a resource (asset) for the difference, which is the *original cost value of the articles on hand.*

407. When furniture and fixtures have depreciated through use, the depreciation is not shown in the investment account but should be charged to a "Reserve for Depreciation" account which is explained in ¶557; or if this account is not kept, it should be charged to the general expense account or directly to profit and loss account.

Rule for Debiting and Crediting Furniture and Fixture Investment Accounts.

408. *Debit furniture and fixture investment accounts for costs: credit for returns.*

409. The various applications of the rule are as follows:

410. Debit the investment account under its appropriate title,—

a. For the value of the property on hand at the beginning of business.

b. For all purchases of furniture and fixtures, including all charges for delivering, installing, etc., until the same is ready for use.

411. Credit the investment account, under its appropriate title,—

c. For all sales of furniture and fixtures at their original *cost* value i. e., *for the original price charged to the account.*

412. Observe that in every instance the account is debited for the *cost* of the furniture and fixtures purchased.

413. Observe that in every instance the account is credited for the *returns* from the property disposed of at the *original cost price.*

414. Transactions Illustrating the Various Applications of the Rule (¶408) for Debiting and Crediting Furniture and Fixtures, Investment Account.

(1) Jan. 1 The following furniture and fixtures were purchased: 1 double mahogany desk, $82.50 (¶410*b*); 1 single desk, $45; 3 chairs, $17.50; 1 typewriter,

$75; 1 filing case, $12.50; 1 copy press, $5; 1 typewriter table, $7.50; 1 rug for office, $20; 1 telephone booth, $7.50. – – JAN. 15. 1 safe, $125. – –JAN. 31. The copy press being found unsuitable, it was disposed of at cost price, $5. (¶411*c*)

Prepare an account showing the original cost value of the furniture and fixtures on hand, with the balance brought down to begin the account for the next fiscal period. (¶415)

ILLUSTRATION 60.

Furniture & Fixtures

19 Jan	1	Mahog. desk	82 50	19 Jan.	31	Copy press	5
	1	Single desk	45		31	Balance	392 50
	1	3 chairs	17 50				
	1	Typewriter	75				
	1	Filing case	12 50				
	1	Copy press	5				
	1	Typewriter table	7 50				
	1	Rug for office	20				
	1	Telephone booth	7 50				
	15	Safe 392.50	125				
			397 50				397 50
Feby.	1	Balance	392 50				

415. The difference between the two sides of furniture and fixtures account shows *the original cost value of the furniture and fixtures on hand* which is a resource that should appear as an item in the statement for resources and liabilities.

416. To close. Follow instructions, "To Close Real Estate Investment Accounts," ¶386.

REPAIRS AND RENEWALS ACCOUNT.

417. Furniture and fixtures repairs and renewals is a companion account of the furniture and fixtures investment account and in some respects closely resembles a real estate expense and income account, except that it seldom shows credit items inasmuch as there is usually no direct income from this kind of property.

417*a*. It is seldom necessary to carry this sort of an account as these items can be charged directly to general expense account, which is advisable under ordinary circumstances. A separate repairs and renewals account should be kept only in case the items are of sufficient number and importance to justify it.

418. The purpose of this account may be extended under the heading "Repairs and Renewals," to include not only the cost of repairs and renewals of furniture

and fixtures, but also similar costs for buildings and machinery, warehouse tools and appliances, delivery equipment, or any other outlays for the maintenance or repairs of property *used in carrying on the business*, when other accounts for that purpose are not kept.

419. Repairs and renewals is always a profit and loss account and in a trading business should appear as a separate item in the profit and loss statement. In a manufacturing business separate repairs and renewals accounts should be kept—one for furniture and fixtures, which should appear as a separate item in the profit and loss statement, and another for buildings, machinery, tools appliances, and other property constituting the "plant" used in the manufacturing department, which should appear in the manufacturing section of the profit and loss statement as will be explained in the chapter on manufacturing accounts in this work.

419*a*. When a "reserve for repairs and renewals" account is set up to meet the cost of repairing or renewing property of any department of the business, the total cost of such repairs and renewals as shown by repairs and renewals account may be debited, at the close of the fiscal period, to the reserve account, which is fully described in ¶ 557*a*.

RULE FOR DEBITING AND CREDITING REPAIR AND RENEWAL ACCOUNTS.

420. *Debit repair and renewal accounts for costs: credit for returns.*

421. The various applications of the rule are as follows:

422. Debit repairs and renewals account, under its proper heading,—

a. For the costs of repairs and renewals of furniture and fixtures, and also warehouse, delivery, office and other equipments, unless separate accounts are kept for these outlays.

b. For the cost of repairs and renewals of buildings, machinery, tools, and all other equipment of the plant in a manufacturing business.

423. Credit repairs and renewals accoun under its proper heading,—

c. For any returns from items charged to the account.

424. TRANSACTIONS ILLUSTRATING THE VARIOUS APPLICATIONS OF THE RULE (¶420) FOR DEBITING AND CREDITING REPAIR AND RENEWAL ACCOUNTS.

JAN. 5. Paid for repairing two old chairs, $2. (¶422*a*) – – JAN. 19. Paid for revarnishing desk, $5. – – JAN. 12. Paid for repairing desk drawer, $1. – – JAN. 26. Paid for repairing typewriter, $7.50. – – JAN. 29. Paid for repainting sign, $4.50.

Prepare an account showing the cost of repairs and renewals of furniture and fixtures for the month, as shown in the following illustration. (¶425)

ILLUSTRATION 61.

Furniture & Fixtures, Repairs & Renewals

Jan 5	Rpg 2 chairs	2	Jan 31	Profit & Loss a/c, to close	20
10	Revarnishing desk	5			
12	Rpg desk drawer	1			
26	Rpg typewriter	7 50			
29	Rpg sign	4 50			
		20			20

425. The difference between the two sides of a "repairs and renewals" account shows the cost of repairs and renewals for the period, which is a *loss* that should appear as an item (or items) in the profit and loss statement.

426. To close. Follow instructions for closing real estate expense and income accounts. (¶397)

EXERCISES IN FURNITURE AND FIXTURES INVESTMENT AND REPAIR AND RENEWAL ACCOUNTS.

427. The following transactions involve both investment and repair and renewal accounts. Prepare ledger accounts for each, applying the rules (¶408, ¶420) in determining the proper debits and credits, and present for approval.

(1) Frank T. Rich, at the opening of his business January 1, had furniture and fixtures on hand valued at $287.20. (¶410*a*) – – JAN. 15. He purchased one single desk, $50; freight on the same, $2.35; drayage from depot to office, 50c. – – FEB. 12. He paid for one rug for office use, $23.75; two chairs, $17.50; one typewriter desk, $24; filing case, $30; hat rack, $6.50. – – FEB. 15. He paid for revarnishing desk, $3.50 (¶422*a*); putting new border on an old rug, $5. – – MARCH 12. He paid for repairing broken chair, $1.75; repairing gas fixtures, $3.60

What did each account show at the close of the fiscal period, March 31?

(2) S. M. Watson & Company purchased on June 25 a second-hand mahogany desk at auction, $29.60. – – JULY 3. They paid for repairs on the desk, $7.35. – – JULY 15. They paid for electric fan, $22.50—installation, $2.25. – – JULY 18. They paid for repairs on clock, $2.50; for a directors' table, $42.50. – – AUG. 31. Paid for typewriter repairs, $4.25; on the same day they paid for a new sign, $16.60. – – DEC. 10. They paid for three new chairs, $18.75; for refinishing two chairs, $2.60.

What did each account show at the close of the fiscal period, December 31?

ARITHMETICAL PROBLEMS—FURNITURE AND FIXTURES INVESTMENTS AND REPAIRS AND RENEWALS.

(1) R. S. Mitchell paid for painting his radiators, $3.25; typewriter repairs, $6.75; bookkeeper's desk, $27.50; two rugs for office, $35; electric light fixtures, $12.50; repairs to electric wiring, $4.80; repair of movable partition, $2.25; hat rack, $5.40; new sign, $24; repainting old sign, $8.75. He disposed of a desk at cost value, $22. He received for rent of typewriter, $12.50.

What is the cost of the furniture and fixtures on hand, and of the repairs and renewals?

(2) The Bates Hardware Company took from stock for their own use one floor truck, $11.50: one pair of scales. $16.75. They purchased two office desks, $84.50; one typewriter, $90; two show cases, $36; one filing cabinet, $45; freight on the same, $3.70. They paid for repairs to shelving and counters, $9.25; repairs on show cases, $2.50. They purchased a typewriter for $80, giving in exchange the old machine at $40, the cost value of which was $90.

What was the cost of furniture and fixtures, and of repairs and renewals for the period?

DELIVERY EQUIPMENT ACCOUNT.

428. Horses and wagons is the name sometimes given to this account. It is kept to show the amount of capital invested in the equipment used to deliver goods to and from the store or warehouse or to customers. It must be distinguished from the delivery expense account described in ¶289.

429. It is a capital investment account, kept for the purpose of showing the *original cost* of the horses, wagons, harness, blankets, automobiles, and whatever else constitutes the equipment used in the delivery of goods. When anything charged to this account is disposed of the account is credited, not for the selling price, but for the *original cost price charged to the account.* The account will, therefore, always show a *resource* (asset) for the difference, which is the *cost value of the delivery equipment on hand.*

430. When delivery equipment has depreciated through use or for any other reason, the depreciation is not shown in this account, but in an account known as a "Reserve for Depreciation" account, which is explained in ¶557*a*; or if such an account is not kept, the depreciation should be charged to general expense account or directly to profit and loss account.

430*a*. In preparing the statement of resources and liabilities, depreciation on property, whether estimated, or shown in a separate reserve account, should be deducted from the balance shown by the investment account, the difference being extended into the resource column. By this method, it will be seen that the depreciation appears on the statement as a *deduction from resources,* and consequently *should not appear as a liability.*

RULE FOR DEBITING AND CREDITING DELIVERY EQUIPMENT ACCOUNT.

431. *Debit delivery equipment account for costs: credit for returns.*

431*a*. Debit delivery equipment under an appropriate heading, for all *costs*.

431*b*. Credit delivery equipment, under an appropriate heading, *at cost price*, for any property charged to this account which is sold or otherwise disposed of.

432. TRANSACTIONS ILLUSTRATING THE VARIOUS APPLICATIONS OF THE RULE (¶431) FOR DEBITING AND CREDITING DELIVERY EQUIPMENT ACCOUNT.

JAN. 1. Paid for two horses, $200 (¶431*a*); one wagon, $50; two sets of harness, $25. – – JAN. 5. Paid for two blankets, $8.50 – – JAN. 25. Paid for one horse, $150. – – JAN. 28. Paid for wagon, $65; harness, $15; – – JAN. 30. Sold one of the horses purchased on January 1, which was found unsuitable, at cost price, $100. (¶431*b*)

Prepare an account showing the cost of the delivery equipment on hand January 31, as shown in illustration 62.

ILLUSTRATION 62.

Delivery Equipment

19					19			
Jan.	1	2 horses	200		Jan. 30	Horse		100
	1	Wagon	50		31	Balance		413 50
	1	2 sets harness	25					
	5	2 blankets	8	50				
	25	Horse	150					
	28	Wagon	65					
	28	Harness 413.50	15					
			513	50				513 50

433. The difference between the two sides of a delivery equipment account shows the *original cost value of the property on hand*, which is a *resource* which should appear as an item in the statement of resources and liabilities.

434. To close. Follow the instructions for closing real estate investment accounts ¶386.

PROFIT AND LOSS STATEMENT.

435. The profit and loss statement is made up from the various ledger accounts showing losses and gains.

436. Profit and loss accounts contain all the facts relating to the costs of expenses and the returns from incomes. These facts are so arranged in the profit and loss statement that the expenses and incomes are shown "in their proper relations." (¶2). They may be shown in detail to any extent desired by the sub-division of accounts, or by the sub-division of the items shown by the different accounts on analysis sheets. Like the trading statement, the profit and loss statement is frequently accompanied and supported by various supplementary statements, exhibits, etc.

437. The final result shown by a profit and loss statement is the *net profit* for the fiscal period represented.

438. The accounts affecting the profit and loss statement are shown in the following list made up from the illustrative accounts showing losses and gains in the preceding pages, as they appear in the trial balance. (Illustration 85) The amounts shown represent the *differences* between the two sides of the various accounts. When both expenses and incomes are shown in the same account, if it is desired to show them separately in the statement, the footings of the account instead of the difference, should be entered on separate lines in the trial balance. An illustration of an account showing both expenses and incomes is the real estate expense and income account. (¶388)

SECTION OF TRIAL BALANCE SHOWING PROFIT AND LOSS ACCOUNTS.

ILLUSTRATION 63.

Sales Expense	315 20	
Freight	65 40	
Administrative Expense	275	
General Expense	85 56	
Insurance Expense	7 50	
Interest	7	
Real Estate, Expense & Income	31 06	
Furniture & Fixtures, Repairs & Renewals	20	

439. The first item shown in the illustration of the profit and loss statement (illustration 64) is the gross trading profit shown by the profit and loss account, which was opened when the journal entry closing the trading accounts, after the trading statement was prepared, was posted to the ledger. This account, therefore, does not appear in the final trial balance shown in illustration 85 or in the section shown in illustration 63.

439*a*. It should be observed that the closing journal entry made after the trading statement is prepared, when posted, will close all the trading accounts in the ledger, and that the gross trading profit transferred to the profit and loss account

equals the difference between the total debit and total credit balances shown by the trading accounts, and that, consequently, when this item is posted it will maintain the equilibrium of debits and credits in the ledger, and that the ledger will be in balance. The posting of the closing journal entry for the trading account simply eliminates these accounts from the ledger and introduces in their stead the item showing the gross trading profit.

440. This form of the profit and loss statement is known as the report form, which is generally preferred for comparative purposes, and for that reason has some advantages for purposes of instruction, as it is somewhat simpler than the technical form shown in illustration 97.

ILLUSTRATION 64.

Profit & Loss Statement January 31, 19 F. A. Raymond

Credits			
Gross trading profit	P & L a/c.		2009 18
Debits			
Selling expense	315.20		
Freight	65.40	380 60	
Administrative expenses		275	
General expenses		85 56	
Insurance		7 50	
Interest		7	
Real Estate repairs and renewals		31 06	
Furniture and fixtures repairs and renewals		20	806 72
Net profit for the month			1202 46

440*a*. Illustration 64 shows the simplest form of the profit and loss statement made up from the *differences* (balances) shown by the profit and loss accounts as they appear in the trial balance, without including any detailed information as to the various items constituting the amount shown.

440*b*. Illustration 65 shows the same statement, with the important items entering into the cost, selling expenses, administrative expenses, and general expenses given in detail. The items can be readily ascertained by referring to the sales expense, administrative expense, and general expense accounts, the amount on the statement being composed of one or more of the items given in the explanation columns of the accounts.

440*c*. *To secure this detailed information* in accounts containing any considerable number of items or extending over the usual fiscal period of one year, it will be necessary to separate them, for each account, on an analysis sheet, which is fully explained and illustrated in ¶490.

ILLUSTRATION 65.

Profit & Loss Statement January 31, 19 F. A. Raymond

Credits			
Gross trading profit P & L a/c.			2009 18
Debits			
Selling Expenses Sales Exp. a/c.			
Sample cases	20.15		
Advertising and premiums	66.65		
Delivery charges	35.		
Salesmens salaries and commissions	130.		
Traveling Expenses	30.90		
Miscellaneous	32.50		
Total	315.20		
Freight	65.40	380 60	
Administrative expenses Adm. Exp. a/c.			
Office supplies	17.50		
Legal advice	10		
Salaries office help	92.30		
Managers salary	150.		
Miscellaneous	5.20	275	
General Expenses			
Light and heat	15.31		
Rent	65.		
Miscellaneous	5.25	85 56	
Insurance		7 50	
Interest		7	
Real Estate repairs and renewals	31.06		
Furniture and fixtures repairs and renewals	20.	51 06	806 72
Net profit for the months			1202 46

PREPARATION OF THE PROFIT AND LOSS STATEMENT.

CREDITS.

440*d*. Explanation. Read carefully ¶435 to ¶440*c* inclusive. The credits are shown first in this (the report) form of the profit and loss statement.

(1) *The gross trading profit, $2009.18*, is the profit shown by the trading statement. (¶242, ill. 40) Other credits, shown by any account in which incomes are entered, should follow this item, as will be shown in later examples.

DEBITS.

(1) When the statement is made up from the differences shown by the profit and loss accounts, the first three accounts should be entered in the order shown on the statement, i.e., selling expenses *first*, administrative expenses *second*, general expenses *third*. Other items may appear in whatever order they occur in the trial balance.

(2) When the *various expenditures* included in the sales, administrative, and general expense accounts are to be given in detail, as shown in illustration 65, they must first be ascertained before the profit and loss statement can be prepared. The method of ascertaining these various expenditures is fully explained in ¶490.

(3) *The net profit for the period* is found by taking the difference between the total debits and the total credits. If the debits are the larger, the difference is the *net loss* for the period.

(4) In preparing the profit and loss statement, refer to the ledger accounts for detailed information, when necessary.

441. Prepare a profit and loss statement like illustration 64, referring to the section of the trial balance for each item as it is entered, and present for approval.

441*a*. Prepare a profit and loss statement like illustration 65, showing on a separate sheet the items named in the ledger accounts which make up the various expenditures shown in the profit and loss statement, and present for approval.

Principles Involved in the Making of a Profit and Loss Statement.

442. Observe that the following principles apply in determining the net profit or the net loss in the profit and loss statement:

(*a*) Any account or item that has *increased* the cost of expenses or *decreased* the returns from incomes has *decreased* the net profit or *increased* the net loss for the period.

(*b*) Any account or item that has *decreased* the cost of expenses or *increased* the returns from incomes has *increased* the net profit or *decreased* the net loss for the period.

443. To find the net trading profit. The gross trading profit *less the selling expenses* gives the *net trading profit*, which is the profit on the goods sold after both cost price and the selling expenses have been deducted.

444. The object of finding the net trading profit is (*a*) to ascertain whether or not the sales have been made on a proper margin of profit, (*b*) to ascertain whether or not the total selling expense is in proper proportion to the total sales made, and (*c*) to permit of a comparison of the net selling profit on the sales of one fiscal period with the net selling profit on the sales of another similar fiscal period.

444*a*. *The difference* between the *net* trading profit and the *gross* trading profit is that the former is the profit *after* the selling expenses have been deducted, while the latter is the profit *before* the selling expenses have been deducted.

444*b*. In the profit and loss statement, illustration 65, the net trading profit is the difference between $2009.18, the gross trading profit, and $380.60, the selling expenses, or $1628.58.

445. Comparisons of the facts shown in a profit and loss statement are usually made on a *percentage basis*. The percentages are found as follows:

(*a*) *The total selling expense* divided by the gross trading profit will give the percentage of the gross trading profit required to meet the selling expenses.

(*b*) *The total administrative expense* divided by the gross trading profit will give the percentage of the gross trading profit required to meet administrative expenses.

(*c*) *The total general expense* divided by the gross trading profit will give the percentage of the gross trading profit required to meet general expenses.

(*d*) The percentage of the gross profit required to meet any other expenses may be found in the same manner.

(*e*) *The total selling expense* divided by the *cost of the merchandise sold* will give the percentage of the cost price which must be added to meet selling expenses. The percentage to be added to the cost price of the merchandise sold to meet administrative or any other expenses may be found in the same manner. These percentages are useful in *fixing the selling prices* of goods.

NOTE.—These percentages must not be confused with the percentages *on capital.*

TO CLOSE LEDGER ACCOUNTS SHOWN IN THE PROFIT AND LOSS STATEMENT BY SEPARATE JOURNAL ENTRIES.

446. When the profit and loss statement has been completed, a journal entry is prepared to close all the accounts in the ledger containing the amounts shown in the statement, the *net profit* or the *net loss* appearing as one or more items in the entry to balance it, which is transferred to the proper side of the undivided profits account in the ledger, or to such capital, reserve, surplus or other accounts as should receive the distribution of all or part of the profits or losses.

447. The purpose of closing the various accounts included in the profit and loss statement is to *indicate the close of a business period*, and thus to eliminate them as open accounts in the ledger, preparatory to their receiving the entries of a new business period. This is the principal reason for closing any account in the ledger.

RULE FOR CLOSING PROFIT AND LOSS ACCOUNTS.

448. *Debit profit and loss accounts showing credit balances. Credit profit and loss accounts showing debit balances.*

448*a*. Illustration 66 shows the correct journal entry to close the accounts included in the profit and loss statement when it is desired to open an *undivided profits account* (¶450) in the ledger. Prepare this journal entry and present for approval.

ILLUSTRATION 66.

Jan. 31, 19

Profit & Loss	To close	2009 18	
Sales Expense			315 20
Freight			65 40
Adm'n Expense			275
Gen'l Expense			85 56
Insurance			7 50
Interest			7
Real Est. Rep's & Ren's			31 06
Fur & Fix. Rep's & Ren's			20
Undivided Profits	For net profit for month		1202 46

448*b*. Undivided profits account may be omitted from the ledger, as explained ¶486*a*.

EXERCISES IN PREPARING PROFIT AND LOSS STATEMENTS.

449. Prepare profit and loss statements for the following profit and loss accounts as they appear on the various trial balances shown, and present for approval. The first example is an exact duplication in form of the profit and loss statements shown in illustrations 66 and 65, the only difference being in the amounts and in the length of the fiscal period, which is one year instead of one month.

(**1**) The profit and loss accounts as they appear in the trial balance of Hughes & Hillen for the fiscal year ending December 31 are shown in illustration 67. The gross trading profit shown by the trading statement for the period is $23,876.40

ILLUSTRATION 67.

Sales Expense	2836 50
Freight	419 98
Administrative Expense	4127 62
General Expense	1541 24
Insurance Expense	226 15
Interest	35 50
Real Estate Expense & Income	260 45
Furniture & Fixtures Repairs & Renewals	43 75

(*a*) Prepare a profit and loss statement showing the net profit for the period, using illustration 64 as a model, and then prepare the journal entry to close the profit and loss accounts in the ledger, and present for approval.

(*b*) An analysis of the sales, administrative, and general expense accounts for the year shows that the items for which these expenditures were made are as follows:

Selling expenses,—sample cases, $90.44; advertising and premiums, $642.20; delivery charges, $426.25; salesmen's salaries and commissions, $1400; traveling expenses, $125.10; miscellaneous, $152.51. Total, $2836.50.

Administrative expenses,—office supplies, $152.16; legal advice, $15; salaries of office help, $815.60; managers' salaries, $3000; miscellaneous, $144.86. Total, $4127.62.

(*c*) Prepare a profit and loss statement showing in detail the selling, administrative and general expenses, using illustration 65 as a model, and present for approval.

General expenses,—light and heat, $315.25; rent, $1200; miscellaneous, $25.99. Total, $1541.24.

NOTE: The journal entry to close the profit and loss accounts are the same for both forms of the profit and loss statement.

(**2**) Negley & Company's gross trading profit shown by the trading statement for the half year ending June 30 is $34,881.18. The various profit and loss accounts appearing in their trial balance of that date are shown in illustration 68.

ILLUSTRATION 68.

Sales Expense	3660 12	
Administrative Expense	6133 56	
General Expense	1938 27	
Insurance Expense	720 20	
Interest		437 25
Real Estate Expense	362 65	
Real Estate Income		1400

(*a*) Prepare a profit and loss statement showing the net profit, using illustration 64 as a model. Then prepare the journal entry to close the profit and loss accounts in the ledger, debiting all accounts showing credit balances and crediting all accounts showing debit balances, and present for approval. Illustration 69 shows the arrangement of the credit accounts showing gains, following the amount of the gross trading profit. The remainder of the statement is similar to illustration 64.

ILLUSTRATION 69.

Profit & Loss Statement June 30, 19 Negley & Co.

Credits		
Gross trading profit	34881 18	
Interest	437 25	
Real Estate Income	1400	36718 43
Debits		
Sales Expense		

(*b*) Analysis sheets made up from the sales expense and administrative expense accounts show the following results:

Selling expenses,—salesmen's salaries, $1600; traveling expenses, $954.50; advertising, $436; delivery expenses, $610; miscellaneous, $59.62. Total, $3660.12.

Administrative expenses,—officers' salaries, $4000; office help, $1400; office supplies, $415.25; miscellaneous, $318.31. Total, $6133.56.

General expenses,—rent, $1800; miscellaneous, $138.27. Total, $1938.27.

(*c*) Prepare a profit and loss statement, using illustration 65 as a model, and present for approval.

(3) The Allen & Briscoe Company close their books annually, December 31. Instead of a single selling expense account, they kept separate accounts with *salesmen's salaries and traveling expenses* (¶268*a–c*), *advertising* (¶268*f*), *delivery expenses* (¶268*g*), and *freight* (¶268*i*). Other selling expense items are charged to the sales expense account. In like manner, instead of a single administrative expense account, they kept separate accounts with *officers and clerks' salaries* (¶301*a*, *b*), and *office supplies and expenses* (¶301*c*), other items being charged directly to the administrative expense account.

At the time of closing, after the trading statement was prepared and the journal entry closing the trading accounts had been posted, with the gross trading profit carried to the credit of the profit and loss account, the ledger contained the following accounts showing profits and losses. Observe that they include *purchase discounts* and *sales discounts*, which are considered by this company as profit and loss accounts. (¶218, ¶219, ¶220*b*, ¶225*b*. ¶226*b*, ¶231*b*)

ILLUSTRATION 70.

Sales Expense		396 31	
Salesmens Salaries & Expense		5160 75	
Advertising		2145 43	
Delivery Expense		739 20	
Freight		181 12	
Administrative Expense		363 78	
Salaries		9341 13	
Office Supplies		1186 61	
General Expense		417 74	
Rent & Taxes		3175	
Purchase Discounts			721 80
Sales Discounts		1839 34	
Expired Insurance		616 17	
Interest			319 50
Discount		76 45	
Real Estate Repairs & Renewals		128 19	
Real Estate Rents			950
Profit & Loss	Gross trading profit		33746 87
	Profits from sale of property		2138 40

a. Prepare a profit and loss statement showing the net profit for the period, using illustrations 65 as a model. There are two items shown in the profit and loss account which should appear separately in the statement.

b. Prepare the journal entry to close the profit and loss accounts in the ledger, debiting all accounts showing credit balances and crediting all accounts showing debit balances. Credit undivided profits account for the difference between the total debit and credit items.

c. What is the net trading profit shown by this statement? (¶443)

d. What percentage of the gross trading profit was required to meet the selling expenses? (¶445*a*)

e. What percentage of the gross trading profit was required to meet the administrative expenses? (¶445*b*)

ARITHMETICAL PROBLEMS—PROFIT AND LOSS ACCOUNTS AND STATEMENTS.

(**1**) If the gross trading profit is $9341.46, and the selling expense $1050.50. what is the net trading profit? (¶445) What percentage of the gross trading profit is the selling expense?

(**2**) If the gross trading profit is $12,736.15, selling expense $1421.50, administrative expense $1850, general expense $315, what percentage of the gross trading profit is required to meet each expense?

(**3**) If the gross trading profit is $18,950, and the total expenses from all sources $6724.75, what percentage of the gross trading profit is required to meet the expenses of the business?

DISTRIBUTION OF UNDIVIDED PROFITS.

450. Undivided profits account is usually kept to show the net profits of each fiscal period, and also to show what disposition has been made of them. Undivided profits is (*a*) credited for the net profits shown by the profit and loss statement and (*b*) debited for the amount of these profits carried to other accounts. If part (or all) of the undivided profits are not distributed, the remainder shows a credit balance in the undivided profits account, until otherwise disposed of. Undivided profits really increase the working capital of the concern to that extent, whether they remain in that account or in a surplus or a reserve account; but these accounts should not be confounded with sinking or redemption fund accounts, which represent funds that are taken out of the working capital of the business.

450*a*. *Not infrequently* undivided profits account is kept so that it shows only the profits of the concern that are *left over* after allotments of the profits have been made to other accounts. This is particularly the case in the accounts of corporations, where the profits are distributed to stockholders on a percentage basis, through a dividend account. The undivided profits account must not be confused with the surplus account which, while similar in its purpose, has a different meaning attached to it in the preparation of profit and loss and financial statements.

451. The disposition of undivided profits is determined entirely by the wishes of the owner of the business. When the business is conducted by an individual or a firm, the profits are usually carried to the credit of the proprietor or partners' capital investment or personal accounts, or both; when conducted by a corporation, they are distributed in whatever manner the board of directors may determine, for the payment of dividends, or for such surplus, reserve or other accounts as may be required to meet the conditions of the business.

452. The distribution of any part of the net profits shown by the undivided profits account is made by journal entry.

Exercises in Distributing Net Profits Shown by the Undivided Profits Account.

453. The following illustrations show the journal entries for the undivided profits as stated in the different examples. Prepare the journal entry for each, and present for approval.

(**1**) The net profit shown by the profit and loss statement of January 31 of F. A. Raymond, as per his instructions, is to be distributed as follows: $200 to be credited to his personal account to balance that account, (illustration 11) and $1002.46 to be credited to his investment account, illustration 10. (¶62*j*)

a. The journal entry to close, per these instructions, is as follows:

Illustration 71.

		31			
	Undivided Profits	To close	1202 46		
	F. A. Raymond	Personal a/c		200	
	F. A. Raymond	Capital a/c		1002 46	

b. If his instructions were to transfer the entire net profit for the period to his investment account, the journal entry would be:

Illustration 72.

		31			
	Undivided Profits	To close	1202 46		
	F. A. Raymond	Capital a/c		1202 46	

c. If it had been his intention to withdraw his net profits, then the best practice would be to credit his personal account instead of his capital investment account, in which case the journal entry would be as follows:

ILLUSTRATION 73.

	31			
Undivided Profits	To close		1202 46	
F. A. Raymond	Personal a/c			1202 46

(2) B. F. Wade & C. E. West are equal partners. Wade's personal account shows a debit balance of $650. West's personal account shows a debit balance of $1000. Their net profit for the period, as shown by the undivided profits account, is $3568, which is to be divided equally between them. Each partner's personal account is to be debited and credited with such an amount as will close it, the remainder to be credited to his investment account.

The following is the journal entry to adjust:

ILLUSTRATION 74.

	31			
Undivided Profits	To close		3568	
B. F. Wade	Personal a/c			650
B. F. Wade	Capital a/c			1134
C. E. West	Personal a/c			1000
C. E. West	Capital a/c			784

(3) The profit and loss statement of the Stilson Machine Company shows net profits at the close of the fiscal year, December 31, of $8586.50, which has been transferred to the credit of undivided profits account. At a meeting of the board of directors, a dividend of 8% of the capital stock of $40,000 was declared, and it was directed that $5000 should be transferred to the surplus account as an addition to the working capital, the remainder, $386.50, to remain as undivided profits.

The journal entry to adjust is as follows:

ILLUSTRATION 75.

	31			
Undivided Profits	To close		8200	
Dividend	8% on $40000.			3200
Surplus				5000

(4) The profit and loss statement of M. G. Nilan shows a net profit of $3160. His personal account shows a debit balance of $156.45. He has instructed his bookkeeper to make a journal entry to balance this account, transferring the remainder to his capital investment account. Prepare the journal entry.

(5) O. P. Hamlin & F. W. Gay are partners in a business in which Mr. Hamlin has a two-thirds interest and Mr. Gay a one-third interest in net profits amounting to $5630.10. Mr. Hamlin's personal account is debited for $445. Mr. Gay's personal account is debited for $556. These accounts are to be credited with such parts of each partner's profits as will balance them, the remainder to be credited to their capital investment accounts. Prepare the proper journal entry to adjust.

(6) The undivided profits account in the books of the M. R. Hale Company show a credit balance of $17319.75. A dividend of 6% has been declared on the capital stock of $50000. Of the remainder, $3000 has been set apart as a "Reserve Fund for Depreciation," and $10000 as a surplus to increase the working capital of the business, the remainder, $1319.75, to remain to the credit of undivided profits account. What is the journal entry to adjust?

JOURNALIZING, POSTING, CHECKING TRIAL BALANCES, ETC.

454. Journalizing is determining the proper accounts to be debited and credited for each transaction. This does not mean that all journal entries must be made in a journal. The proper accounts to be debited and credited are determined as the entries are made, whether in the cash book, sales book, purchase book, note books, journal, or any other book used as a posting medium. In a broad sense, journalizing is the classification of transactions.

454*a*. The proper accounts to be debited and credited are determined by applying the rules of bookkeeping. (¶18) These rules are set forth in detail in the various accounts illustrated in this text.

455. Posting is transferring to the ledger the debit and credit items from the different books in which entries are made. All debit items in the different books are posted to the *debit side* of the account named in the ledger and all credit items are posted to the *credit side* of the account named in the ledger.

455*a*. *Books of original entry* are those books which contain the original or first entries of transactions. All such books do not necessarily contain items to be posted to the ledger, as the items may first be transferred to some other book—for instance when notes receivable and payable are transferred from the note book to the journal before posting. Books containing items to be posted to the ledger are known as *posting mediums*.

456. Checking. There are different methods of checking accounts. A simple and effective method is to check each item in the ledger thus (.) with a pencil on the double line just to the left of the amount, and then to check the entry in the book from which it is posted thus (✓). The items are checked in the order in which they occur in the books from which they are posted. Other methods of checking will be described and illustrated in the various sets included in this work.

TRIAL BALANCES, INVENTORIES, STATEMENTS, ETC.

457. The system of double entry bookkeeping requires that the debits and credits of each transaction must be *equal in amount*, that where one account is debited for a given amount some other account is credited for an equal amount. It follows that if the debits and credits of each transaction are equal in amount, the total debits and credits, as exhibited in all the ledger accounts, must be equal in amount. This equality of debits and credits is not necessarily maintained by entering the *same amounts* on each side of the ledger, as one debit may equal the sum of a number of credits and vice versa.

458. Taking a trial balance means to list or schedule the accounts in the ledger, or ledgers, remaining open at the end of a certain specified day, giving the name and the debit or credit balance of each account, and showing an equal aggregate sum of debits and credits. Accounts are usually entered in the trial balance in the order in which they occur in the ledger. If the debit side of the account is the larger, the difference is placed in the debit column of the trial balance, and vice versa.

458*a*. If the total debits and credits shown by the footings of the trial balance are equal, it proves only that all debit items have been posted to the debit side of the ledger, and that all credit items have been posted to the credit side of the ledger; but it does not prove that each account in the ledger is correct, as errors may have been made in journalizing or in posting to the wrong account in the ledger, which would not disturb the equality of debits and credits. Such errors are usually found by checking or when the monthly statements of account, which are usually issued to all debtors and received from all creditors, are compared with the accounts of the party receiving them. Accounts that balance should be omitted from the trial balance.

458*b*. Trial balances should be taken monthly or quarterly, preferably monthly.

459. The object of taking a trial balance is two-fold, first to ascertain whether or not the debits and credits in the ledger are equal, and second to ascertain the results shown by each account, and from these results *as shown by the final trial balance for the fiscal period* to prepare the various statements exhibiting the condition of the business at the close of the fiscal period.

460. Each account shows one of four different results, namely, a *resource*, a *liability*, a *loss*, or a *gain*. They may be divided into two general classes, those showing resources and liabilities and those showing losses and gains. A single account should never show more than one result in the trial balance. Losses and gains are usually referred to as *profits and losses*. Profits and losses have already been described. (¶251)

460*a*. Occasionally an account will show an exception to the foregoing rule. Offsetting accounts, such as reserve and contingent accounts, show results that are somewhat different. These accounts and their uses will be fully explained in a separate chapter.

461. A resource (or asset) is anything of value belonging to a person, firm or corporation, such as cash, property, or debts owed by others. *Resources* refer to money or other property that can be readily converted into current funds to meet the payment of bills in a going concern. *Assets* refer more particularly to the property of a deceased person, or to the property of an insolvent or bankrupt which is applicable to the payment of his debts or liabilities.

461*a*. *Current resources* are those that pass more or less continuously in the course of business, constituting the *working capital*, particularly those that are available to meet current obligations, such as cash, notes and accounts receivable, etc.; *fixed resources* are those represented in more permanent investments, such as real estate, delivery equipment, furniture and fixtures, etc. Fixed resources are closely identified with capital investment accounts.

462. A liability is a debt owing by a person, firm or corporation.

462*a*. *Current liabilities* are those that are to be met from current funds.

463. The final trial balance at the close of the fiscal period should not be taken until (*a*) all the transactions which properly belong to that period have been entered in the books and included in the results shown by the various accounts, and (*b*) all *inventories*, not only of merchandise but also of other property on hand and of accrued debts owing to us and to others not shown on the books, have been prepared.

464. Inventories. *The merchandise inventory* is a statement or schedule of merchandise on hand or in stock. This inventory is fully described in ¶169–¶175 inclusive, and is the only inventory to be included in the principal inventory account, which is a trading account and affects the trading statement.

465. Other inventories consist of (*a*) all material, supplies and other property on hand that has been charged to a trading or a profit and loss account, which has not been used up or otherwise disposed of in the fiscal period in which it was purchased, and (*b*) of interest, taxes, rents, commissions, or other expenses and incomes *which have accrued at the close of the fiscal period*, but which are not entered on the books and frequently are not due. For this reason this class of inventories are known as *non-ledger* inventories.

465*a*. Real estate, stocks, bonds, machinery, furniture, fixtures, materials and supplies which are included in the various ledger accounts showing the *original cost of the property on hand*, may be inventoried when there is a considerable increase or decrease between the original cost value and the present market or selling value of the property, if it is desired to include such property at its present value in a statement of the resources of a business.

465*b*. When property on hand is inventoried above or below its original cost value, the difference, if a loss, should be debited to a "reserve for depreciation" account; if a gain, to a "reserve for appreciation" account. An owner, if an individual, can do as he pleases in regard to increasing or decreasing the inventory value of the property, so can partners providing they agree, but it should be noted that a corporation cannot declare a dividend legally from a profit of this kind unless the property is sold and the profit actually realized.

466. The object of taking inventories of property *included in the cost* of purchases (the merchandise inventory) and of materials and supplies (trading and profit and loss accounts) is to eliminate from the accounts representing these costs those items which do not enter into the cost of the goods sold or of the materials and supplies used up during the fiscal period in which they were purchased. *The object of taking non-ledger inventories* (¶465) is just the opposite, the purpose being to include them in the accounts they affect which already appear in the ledger without them, so that in both instances the total resources and liabilities, losses and gains, net profits and losses, etc., may be accurately ascertained and shown in the various statements made up at the close of the fiscal period.

466*a*. All inventories affecting profit and loss accounts should be avoided as far as possible by holding the books open until all items belonging to the fiscal period represented are entered in the usual way and included in the final trial balance taken preparatory to making up the various statements. Every bookkeeper or accountant who has had any extended experience knows, however, that this is almost impossible in a business of any magnitude, and that for many such items the easiest method to dispose of them is to treat them as inventories.

467. All inventories of property on hand or of debts owing to us are *resources*; all debts owing to others are *liabilities*.

468. Non-ledger resource and liability inventories relate principally to profit and loss accounts showing expenses and incomes. When an expense account is subdivided into separate accounts, each item in the inventory affects the account in which it was originally charged.

468*a*. *Resource inventories* affecting profit and loss accounts consist of (1) the cost value of any material, supplies, or other property on hand (not used up) at the close of the fiscal period, which was charged to a profit and loss account, (2) the unexpired value of any use or service at the close of the fiscal period which was charged to a profit and loss account (¶461) and (3) accrued interest, rent, and commissions, etc., owing from others and not entered at the close of the fiscal period.

468*b*. *Liability inventories* affecting profit and loss accounts consist of (1) unpaid salaries, commissions, traveling expenses, wages, freight, express or drayage bills, rent, or any other unpaid expense incurred in and not paid or entered at the close of the fiscal period, and (2) accrued interest, rent, taxes, commissions, etc. owing to others and not entered at the close of the fiscal period.

468*c*. *Separate accounts* should be kept, one for *sundry resource inventories* in which all such inventories may be grouped, the account affected being indicated in the explanation column, and another for *sundry liability inventories*, the different accounts affected being similarly indicated. Separate accounts for each inventory taken can be opened, if it is so desired.

Rules for Debiting and Crediting Resource Inventories Affecting Profit and Loss Accounts.

469. *Debit*, by journal entry, **sundry resource inventories** under one or separate headings, *at the close of each fiscal period*, for the cost value of all (each) inventories on hand and credit the profit and loss account to which the items were charged.

470. *Credit*, by journal entry, **sundry resource inventories** under the proper heading, *at the beginning or close of the next fiscal period*, for all (each) inventories debited to this account at the close of the last preceding fiscal period and debit each account which was credited at that time.

471. Transactions Illustrating the Above Rules.

Resource inventories. At the close of the fiscal period, December 31, inventories were taken of the various materials and supplies on hand, the total amount of each inventory being as follows: sales expense account, $36.50; administration expense, $24.19; general expense, $16.50; accrued interest receivable, $14.50. (¶359*m*)

Journal entry, rule ¶469.

Illustration 76.

December 31, 19

Sundry Resource Inventories	91 69	
Sales Expense		36 50
Administrative Expenses		24 19
General Expense		16 50
Interest		14 50

471*a*. The above journal entry, when posted, will show the sundry resource inventories account as follows, at the close of the fiscal period. The amount of each inventory could be shown separately on the trial balance or the total amount shown by the footing of the account (91.69) could be inserted. The account always shows a resource.

ILLUSTRATION 77.

Sundry Resource Inventories

Dec. 19 31	Sales Expense	36 50		
31	Adms. Expense	24 19		
31	Genl Expense	16 50		
31	Interest	14 50		

Journal entry, rule ¶470.

ILLUSTRATION 78.

January 1, 19

	Sales Expense	36 50	
	Administrative Expense	24 19	
	General Expense	16 50	
	Interest	14 50	
	Sundry Resource Inventories		91 69

471*b*. The above is the journal entry for crediting the sundry resource inventories account *at the beginning of the next fiscal period*, although it could properly be made at any time during or at the close of the next fiscal period. It will be noted that this journal entry is just the opposite of the journal entry illustrating rule ¶469, the object being to transfer back into the proper accounts the amounts of the various inventories, so that the various expenses may be shown in the fiscal period in which the materials, supplies, etc., were used. (¶468*a*) The inventories account balances when the items are posted, and it should then be ruled up and footed, as shown in the following illustration.

ILLUSTRATION 79.

Sundry Resource Inventories

Dec. 19 31	Sales Expense	36 50	Jan. 19 1	Sales Expense	36 50
31	Adms. Expense	24 19	1	Adms. Expense	24 19
31	Genl Expense	16 50	1	Genl Expense	16 50
31	Interest 91.69	14 50	1	Interest	14 50
		91 69			91 69

471*c.* Instead of entering the inventories separately in the ledger account, as shown in illustrations 77 and 79, they may be entered in one amount, as shown in illustration 80, in which case the amount of each inventory can readily be ascertained by referring to the journal entry.

ILLUSTRATION 80.

Sundry Resource Inventories

19 Dec. 31	Sundry Inventories		91 69	19 Jan. 1	Sundry Inventories		91 69

RULE FOR DEBITING AND CREDITING LIABILITY INVENTORIES AFFECTING PROFIT AND LOSS ACCOUNTS.

472. *Debit* by journal entry, **sundry liability inventories** under the proper heading, *at the beginning or close of the next fiscal period,* for all inventories credited to this account at the close of the last preceding fiscal period, and debit each account which was credited at that time.

473. *Credit* by journal entry, **sundry liabilities inventories** under one or separate headings, *at the close of each fiscal period,* for the amount owed for expenses which have accrued, and which have not been entered on the books debiting the proper accounts.

474. TRANSACTIONS ILLUSTRATING THE ABOVE RULES.

Liability inventories: At the close of the fiscal period, December 31, inventories for unpaid expense bills were as follows: accrued interest payable, $36.25 (358*f*); accrued taxes, $46; unpaid rent, $75.

Journal entry, rule ¶473.

ILLUSTRATION 81.

December 31, 19

Interest		36 25	
Rent & Taxes	75. + 46.	121	
Sundry Liability Inventories			157 25

474*a.* The following illustration shows the ledger account at the close of the fiscal period, when the above journal entry is posted. This account then always shows a liability.

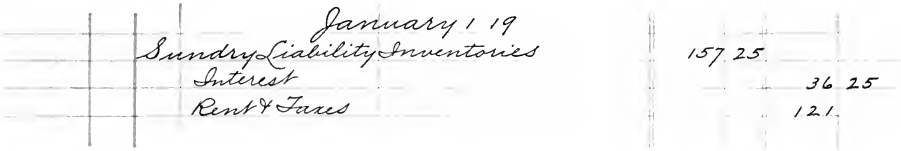
ILLUSTRATION 82.

Sundry Liability Inventories.

19 Dec. 31	Interest		36 25
31	Rent & Taxes		121

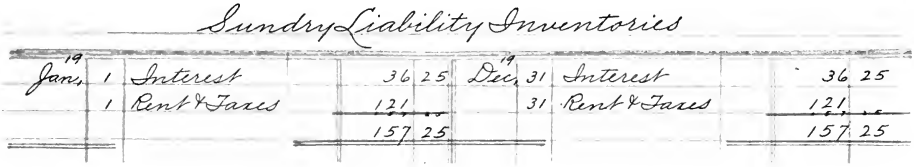
Journal entry, rule ¶472.

ILLUSTRATION 83.



474*b*. The above is the journal entry for debiting the sundry liability inventories account at the beginning of the next fiscal period. The entry could properly be made at any time, either during or at the close of the next fiscal period. Observe that the journal entry has the effect of placing the various inventories back in the accounts to which the items were originally charged, *in the fiscal period in which the expense was incurred.* When the account balances, it should be ruled and footed.

ILLUSTRATION 84.


Sundry Liability Inventories
19 Jan. 1 Interest 36 25
1 Rent & Taxes 121
157 25
19 Dec. 31 Interest 36 25
31 Rent & Taxes 121
157 25

474*c*. The total of the liability inventories may be entered in the ledger account instead of each one separately, as shown in illustration 80 for resource inventories.

CLOSING THE BOOKS, STATEMENTS, ETC.

475. Statements. There are three principal statements usually prepared from the final trial balance, (*a*) the trading statement, described in paragraphs 233–250, (*b*) the profit and loss statement, described in paragraphs 435–453, and (*c*) *the statement of resources and liabilities* (¶487), which consists of a list of all the resources and liabilities of the concern, as shown by the books after all accounts showing gains and losses have been closed and the net profit or the net loss has been transferred to the proper capital, undivided profits, surplus and reserve accounts.

476. The trading and the profit and loss statements which are shown separately in illustrations 40 and 65 are usually combined and made up as a single statement, which includes the distribution of the net profit or the disposition of the net loss. Such a statement is really divided into *three* sections, the *first* section showing the trading statement, the *second* section showing the profit and loss statement, and the *third* section showing the distribution of the net profits or the disposition of the net loss.

477. When the trading and profit and loss statements are combined into one statement, it is customary to prepare therefrom a single journal entry to close not only the trading and the profit and loss accounts included in the statement, but also to dispose of the net profit or the net loss, as shown in the distribution section of the statement. Illustration 88 shows such an entry.

478. Separate journal entries for each section of the combined trading and profit and loss statement may be made, one for the first section to close the accounts included in the trading statement, one for the second section to close the accounts included in the profit and loss statement, and one for the third section to transfer the net profit or the net loss to the proper capital, surplus or reserve accounts. This method is illustrated in the journal entries shown in illustrations 41, 42, 66, 71, etc.

478*a*. *For beginning students,* a separate journal entry for each section is preferable, as it makes a distinct separation of the various accounts included in each section of the complete trading and profit and loss statement, and besides, it conforms with the necessary practice when the conditions described in the following paragraphs (¶479, ¶480) exist, when it is not convenient to combine them in one entry for the entire statement.

479. Some accountants and business men prefer to have formal trading and profit and loss accounts opened in the ledger at the time of closing the books, each showing the same debit and credit items as are shown in the trading and in the profit and loss statements, on the theory that all items appearing in these statements should be supported by corresponding accounts in the ledger. When this plan is followed, these accounts are opened and closed at the time of closing the ledger and remain closed until the next closing of the ledger, unless current items of loss or gain not properly belonging to any other account should be entered into the profit and loss account during the period. (¶248, ¶448)

480. In very large concerns having many accounts, it is practically necessary, on account of their size, to make separate statements for the trading accounts and the profit and loss accounts, as shown in illustrations 40 and 65, as well as for the dis-

tribution of the net profit or loss. This is particularly true of the statement showing the distribution of the net profit to the proper capital or reserve accounts, which in corporations must be determined by action of the board of directors. Not infrequently this action is not taken until several days after the close of the fiscal period.

Principles Involved in Determining the Results Shown by the Various Accounts in the Trial Balance.

481. Each account in the ledger (excepting those referred to in ¶460*a*) shows one of four different results, as stated in ¶460—a resource, a liability, a loss, or a gain. *Debit* items in the ledger show *resources* or *losses*: *credit* items in the ledger show *liabilities* or *gains*.

482. A study and comparison of the following principles will assist greatly in an understanding of the accounts shown in a trial balance:

a. All *resources* are *debits*, and are invariably found on the debit side of the ledger.

b. All *losses* are *debits*, and are always found on the debit side of the ledger.

c. Losses always result in a *decrease* in the *resources* or an *increase* in the *liabilities*.

d. In every instance when an account is debited, the resources or losses are increased or the liabilities are decreased.

e. All accounts showing losses have decreased the resources or increased the liabilities, and consequently, have decreased the net capital or increased the net insolvency.

f. The total losses, if the larger, less the total gains, will give the net loss, and consequently, the net decrease in the resources or the net increase in the liabilities.

g. All *liabilities* are *credits*, and are invariably found on the credit side of the ledger.

h. All *gains* are *credits* and are always found on the credit side of the ledger.

i. Gains always result in an *increase* in the *resources* or a *decrease* in the *liabilities*.

j. In every instance when an account is credited, the liabilities or gains are increased or the resources are decreased.

k. All accounts showing gains have increased the resources or decreased the liabilities, and consequently, have increased the net capital or decreased the net insolvency.

l. The total gains, if the larger, less the total losses, will give the net gain and consequently, the net increase in the resources or the net decrease in the liabilities.

483. To take a trial balance. When all transactions and items belonging to the period have been entered and posted, as stated in ¶463, list the ledger accounts as instructed in ¶458. *The final trial balance* taken from the accounts illustrated on the preceding pages is shown in illustration 85.

ILLUSTRATION 85.

Trial Balance January 31, 19 F. A. Raymond

	Ledger page			
R	8	Accounts Receivable	3667 50	
L	9	Accounts Payable		4527 22
O	10	F. A. Raymond Capital a/c.		15807
R	11	F. A. Raymond Personal a/c.	200	
R	15	Notes Receivable	900	
L	18	Notes Payable		1500
R	21	Cash	2444 21	
T	24	Purchases	3156 47	
T	27	Sales		7025 11
T+R	29	Inventory (Dec 31)	7516 45	
T	32	Warehouse Supplies	61 35	
T	33	Warehouse Labor	120	
T	34	Purchase Discounts		173 51
T	36	Sales Discounts	171 64	
L	49	Sales Expense	315 20	
L	51	Freight	65 40	
L	52	Administrative Expense	275	
L	53	General Expense	85 56	
R	54	Insurance Unexpired premiums	82 50	
L	55	Insurance Expense	7 50	
L	57	Interest	7	
R	58	Real Estate Investment	9100	
L	59	Real Estate Expense & Income	31 06	
R	60	Furniture & Fixtures	392 50	
L	61	Furniture & Fixtures Repairs & Renewals	20	
R	62	Delivery Equipment	413 50	
			29032 84	29032 84

484. The accounts contained in the final trial balance, illustration 85, are entered in the order in which they appear in the preceding pages, to correspond with the order in which they are usually taken from the ledger. (¶458) Illustration 86 shows the same accounts arranged in groups—one for the trading, another for the profit and loss, and the third for the resource and liability statements, in the order in which they usually appear in those statements. This is sometimes done to facilitate the preparation of the statements, and is valuable in assisting the student to distinguish between the various accounts. Note that the merchandise inventory account appears not only in the trading statement, but also in the statement of resources

and liabilities. The statement in which each account appears is also indicated by letters on the left-hand margin of the trial balance in illustration 85.

484*a*. Observe the following distinctions at the time of closing the books between the merchandise inventory taken at the close of the preceding fiscal period and the inventory taken at the close of the present fiscal period:

(1) That the inventory of the preceding period is the only one which at the time of closing the books is shown on the face of the ledger and in the trial balance, and that it is used in making up the trading statement, but that it does not appear in the statement of resources and liabilities.

(2) That the inventory taken at the close of the present period does not appear in the trial balance, and will not be shown on the face of the ledger until after the closing entry for the period has been posted, but that it does appear in the statement of resources and liabilities.

(3) Note in other words that while both inventories appear in the trading statement, one appears in the trial balance but not in the statement of resources and liabilities, and the other appears in the statement of resources and liabilities but not in the trial balance.

ILLUSTRATION 86.

TRIAL BALANCE, JANUARY 31, 19 , F. A. RAYMOND.

P+L	Cash	2444.21	
	Accounts Receivable	3667.50	
	Notes Receivable	900.	
	Real Estate Investment a/c	9100.	
	Furniture & Fixtures	392.50	
	Delivery Equipment	413.50	
	Insurance - Unexpired Premiums	82.50	
	F. A. Raymond, Personal	200.	
	F. A. Raymond, Capital		15807.
	Notes Payable		1500.
	Accounts Payable		4527.22
T	Mdse. Inventory	7516.45	
	Purchases	3156.47	
	Warehouse Labor	120.	
	Warehouse Supplies	61.35	
	Sales Discount	171.64	
	Sales		7025.11
	Purchase Discount		173.51
P+L	Selling Expense	315.20	
	Freight	65.40	
	Administrative Expense	275.	
	General Expense	85.56	
	Insurance Expense	7.50	
	Real Estate Expense & Income	31.06	
	Furniture & Fixtures Repairs & Renewals	20.	
	Interest	7.	
		29032.84	29032.84

COMBINED TRADING AND PROFIT AND LOSS STATEMENT.

485. Full instructions for preparing the trading statement and the profit and loss statement separately are given in preceding chapters, beginning with ¶233 and ¶435. Illustration 87 shows the trading and profit and loss statements combined into a single statement, including the distribution of the net profit.

ILLUSTRATION 87.

TRADING AND PROFIT & LOSS STATEMENT, JANUARY 31, 19 . F. A. RAYMOND.

	Returns				
Gross sales				7124.38	
Less Rebates and allowances			35.14		
Goods returned			64.13	99.27	7025.11
Deduct Sales discounts					171.64
Net returns from sales					6853.47
	Costs				
Inventory, December 31, 19				7516.45	
Purchases			3224.03		
Less Rebates and allowances		27.40			
Goods returned		40.16	67.56	3156.47	
Add Warehouse supplies				61.35	
Warehouse labor				120.	
Total cost of purchases				10854.27	
Deduct Purchase discounts				173.51	
Net cost of purchases				10680.76	
Less Inventory, January 31, 19				5836.47	
Cost of merchandise sold					4844.29
Gross trading profit					2009.18
	Expenses				
Selling expenses	Sales Ex. a/c				
Sample cases			20.15		
Advertising and premiums			66.65		
Delivery charges			35.		
Salesmen's salaries and commissions			130.		
Traveling expenses			30.90		
Miscellaneous			32.50		
		Total	315.20		
Freight			65.40	380.60	
Administrative expenses	Adm. Ex. a/c				
Office supplies			17.50		
Legal advice			10.		
Salaries office help			92.30		
Manager's salary			150.		
Miscellaneous			5.20	275.	
General expenses					
Light and heat			15.31		
Rent			65.		
Miscellaneous			5.25	85.56	
Insurance				7.50	
Interest				7.	
Real estate repairs and renewals				31.06	
Furniture and fixtures repairs and renewals				20.	806.72
Net profit for month to F. A. Raymond's capital a/c					1202.46

485*a*. *Review previous instructions* for preparing trading and profit and loss statements, and then prepare a combined trading and profit and loss statement from the trial balance, as shown in illustrations 85 and 86, using illustration 87 as a model, and present for approval.

Closing the Ledger by a Single Journal Entry.

486. Illustration 88 shows the journal entry made up from the final trial balance and the inventories at the date of closing, to close all accounts in the ledger except those showing resources and liabilities, including reserve surplus, undivided profits and ownership accounts. This journal entry is, in fact, the journal entries shown in illustrations 42, 66 and 71, combined into a single journal entry.

Illustration 88.

January 31, 19

Sales	To close	7025	11		
Inventory	Jan 31,	5836	47		
Purchases Discts	To close	173	51		
Purchases	.			3156	47
Inventory	Dec 31,			7516	45
Warehouse Supplies	To close			61	35
Warehouse Labor	.			120	
Sales Discounts	.			171	64
Sales Expense	.			315	20
Freight	.			65	40
Adm'n Expense	.			275	
Gen'l Expense	.			85	56
Insurance Expense	.			7	50
Interest	.			7	
Real Est Exp & Incd	.			31	06
Fur & Fix, Rep & Rnls	.			20	
F A Raymond Cap'l,	Net profit for the mo.			1202	46

486*a*. *When a single journal entry* is made to close the ledger, as shown in the above illustration, neither a trading nor a profit and loss account is opened in the ledger. This method has become the rule, as the opening of the accounts mentioned is considered to be unnecessary.

486*b*. *Accounts in the ledger may be closed* by transferring the differences shown by the various trading and loss and gain accounts to the "trading" or the "profit and loss" accounts after the old method of closing the ledger. When this method is followed, the trading and profit and loss accounts should be opened. This method is obsolete, however, and is not approved by accountants.

486*c*. The illustrations underneath show the form of the profit and loss statement when the net profit is divided between partners equally, and the part of the journal entry which distributes the net profit to the proper accounts. It is assumed that F. A. Raymond and John Patton are equal partners, each entitled to one-half of the net profits.

ILLUSTRATION 89.

Net profit for the month		1202.46
F. A. Raymond's capital a/c, 1/2 profit,	601.23	
John Patton's capital a/c, 1/2 profit,	601.23	
	1202.46	1202.46

In the journal entry, instead of "F. A Raymond Capital, for net profit, $1202.46," write the following:

ILLUSTRATION 90.

F A Raymond Cap. a/c.	½ profit for mo.	601	23
John Patton Cap. a/c.	½ . . .	601	23

486*d*. Assuming that the business was conducted by a corporation, illustrations 91 and 92 show the net profit distributed on the statement to dividend, surplus, reserve and undivided profits accounts, with the necessary changes in the journal entry to correspond.

ILLUSTRATION 91.

Net profit for the month		1202.46
Dividend 3% on $15000	450.	
Surplus	600.	
Reserve for depreciation	100.	
Undivided profits	52.46	
	1202.46	1202.46

ILLUSTRATION 92.

Dividend No. 1	450	
Surplus	600	
Reserve for Depreciation	100	
Undivided Profits	52	46

486*e*. The principal reasons for closing the various trading and profit and loss accounts in the ledger at the close of the fiscal period are, as stated in ¶247 and ¶447: (*a*) to indicate the close of a business period and (*b*) to eliminate them as open accounts in the ledger, since their results have been disposed of in the net profit or the net loss for the period. After the closing journal entry is posted, the ledger is again in its primal condition, showing only *resources* and *liabilities*.

STATEMENT OF RESOURCES AND LIABILITIES.

487. After the trading and profit and loss statement is completed, the statement of resources and liabilities is prepared. This statement is made up from the resources and liabilities shown on the trial balance and the *inventories* of resources and liabilities. Study illustration 93 carefully. Accountants in practice usually make the statement of resources and liabilities first, and then find what the net profit or loss should be, thus making the profit and loss statement prove the statement of resources and liabilities, although this would seem to be out of the logical order, because it is apparent that the net profit or loss affects the resources and liabilities rather than that the resources and liabilities affect the net profit or the net loss.

487*a*. *The resources* are arranged in two groups, one including the *current resources* arranged in the order of their availability for the payment of bills, and the other including the more permanent investments, which are designated as *fixed* resources. The order in which the accounts showing fixed resources appear is without reference to their importance in paying bills.

ILLUSTRATION 93.

Statement of Resources and Liabilities January 31, 19 F. A. Raymond

Resources			
Cash		2444 21	
Inventory January 31, 19		5836 47	
Notes receivable		900	
Accounts receivable		3667 50	
Total current resources			12848 18
Insurance — unexpired premiums			82 50
Property and equipment			
Real estate and buildings		9100	
Furniture and fixtures		392 50	
Delivery equipment		413 50	9906
Total resources			22836 68
Liabilities			
Notes payable		1500	
Accounts payable		4527 22	
Total liabilities			6027 22
Net resources			16809 46
Represented by —			
F. A. Raymond Capital Acct. Dec 31, 19	15807		
Add profit for January	120246	17009 46	
Less F. A. Raymond's personal account		200	16809 46

487*b*. *The current liabilities* are likewise given precedence in the order of their importance. Other liabilities, such as bonds or mortgages payable, which are more remote as to the time of payment, are frequently designated as "fixed liabilities," which usually appear, however, in connection with the business of a corporation, and therefore are not included in the illustration.

488. The difference between the total resources and the total liabilities shows the *net resources* or the *net liabilities* of the concern, which must equal the net capital or the net insolvency at the close of the last fiscal period plus the net profit or minus the net loss for the present period.

488*a*. *Observe that the difference* between the total resources and the total liabilities equals the *net resources*, which represents the owner's equity or ownership in the business and is shown by the amount of his capital at the beginning of the period represented in the statement plus the net profit for the period, or minus the net loss for the period. The illustration shows the personal account of the proprietor deducted from his investment, the difference equaling the net resources, i. e., the net capital.

488*b*. The net capital represented in the ownership accounts may properly be classed as a *secondary* liability of the concern. After all creditors have been paid, the capital accounts show *what is left* for the owner; but to say that the capital of a concern is a liability would be equivalent to saying that the owner of the business owes himself the amount of his net capital. Read chapters on ownership accounts, ¶55 and ¶69.

Exercises in Preparing Combined Trading and Profit and Loss Statements and Statements of Resources and Liabilities.

489. Prepare a trading and profit and loss statement and a statement of resources and liabilities from each of the trial balances shown, and present for approval. Example two is almost an exact duplication of the trial balance shown in illustration 85, except that the business is owned by a firm instead of a single proprietor; therefore, illustrations 87, 88, 90 and 93 may be used as models in the preparation of the statements and the journal entry.

(**1**) Prepare a trading and profit and loss statement, including detailed information relating to purchases and sales (see ¶242*a*-2 and 3; also ¶242*a*-8), with journal entry to close, and a statement of the resources and liabilities shown on the trial balance (illustration 85), including the merchandise inventory of January 31 of $5836.47.

(**2**) The trial balance of Hicks & Anthony for the year ending December 31, when the inventory of the merchandise on hand at that date was $9524.15, showed the following debits and credits:

Accounts receivable	7946.27	
Accounts payable		6423.19
N. W. Hicks capital a/c		11174.93
N. W. Hicks personal a/c	1200.	
A. R. Anthony capital a/c		11174.92
A. R. Anthony personal a/c	1150.	
Notes Receivable	1690.	
Notes Payable		2346.12
Cash	916.36	
Purchases	12618.35	
Sales		29341.37
Inventory	19444.50	
Warehouse supplies	221.50	
Warehouse labor for the year	1560.45	
Purchase Discounts		821.76
Sales Discounts	1425.80	
Sales Expense	2436.	
Administrative Expense	1833.75	
General Expense	721.60	
Insurance (Unexpired Premiums)	61.50	
Insurance Expense	528.37	
Interest	72.12	
Real Estate and Building	6500.	
Real Estate Expense	114.50	
Furniture and Fixtures	286.90	
Delivery Equipment	554.32	
	61282.29	61282.29

ANALYSIS SHEETS.

490. Analysis sheets have been referred to a number of times in the preceding pages. "Analysis sheet" is a general term applied to any working paper used for the purpose of analyzing or separating the various items appearing in an account. They have no set form or arrangement, but may be designed and ruled up for whatever purpose desired. An analysis sheet may contain any number of columns required for the purpose intended.

490*a*. Two forms of an analysis sheet are shown—one separating into groups the various items shown in a single account and the other showing the cumulative additions to the items shown in the account month by month. These forms can be used to analyze any account, as they admit of expansion to any degree necessary.

ILLUSTRATION 95.

General Exp

Jan. 19	2	Coal	3.50
	2	Postage	1.25
	5	Telegrams	1.60
	6	Postage	2.
	7	Coal	3.50
	11	Gas bill	4.50
	12	Cleaning	2.50
	15	Telegrams	.55
	20	Postage	1.50
	21	Telephone	2.55
	21	Rent	60.
	24	Postage	1.25
	24	Cleaning	1.75
	28	Elec. light	1.60

Analysis Expense a/c for January 19

Postage Telegrams and Telephone	Light and Heat	Miscellaneous
1.25	3.50	2.50
1.60	3.50	.60
2.00	4.50	1.75
.55	1.60	64.25
1.50	13.10	13.10
2.55		10.70
1.25	Total	88.05
10.70		

490*b*. The illustration on the left shows a section of the general expense account for the month. The illustration on the right shows the items separated into groups. These groups might be extended indefinitely, if desired, with a separate column for each particular item. The same form could be used for the analysis of any account for any length of time, the number of columns in the analysis sheet being determined by the number of groups into which the items are to be divided.

ILLUSTRATION 96.

ANALYSIS SHEET

Illustrating General Expense Account.

Items	Month of Jan.	Month of Feb.	Total two mos. to Feb. 28	Month of Mch.	Total three mos. to Mch. 31
Coal	7.00	11.20	18.20	10.00	28.20
Vehicle License	4.50		4.50		4.50
Electric Light	2.10	2.05	4.15	1.80	5.95
Gas	8.40	9.00	17.40	7.50	24.90
Stationery & Printing	11.50	6.00	17.50	12.50	30.00
Postage	5.00	6.00	11.00	7.50	18.50
Cleaning office	2.50	2.50	5.00	2.50	7.50
Repairing chairs	1.75		1.75	.25	2.00
Rent	90.00	90.00	180.00	90.00	270.00
Telephone	3.75	4.15	7.90	3.75	11.65
Telegrams	1.20	.85	2.05	.60	2.65
City Directory	6.00		6.00		6.00
Street car tickets		2.25	2.25	2.00	4.25
Brooms & Mops		1.50	1.50		1.50
Soap		2.50	2.50		2.50
Cr. Sale of carbon paper		1.00	1.00		1.00
	143.70 x	137.00	280.70 x	138.40	419.10 x

Items marked "x" would agree with balance of general expense as shown by the trial balances of these dates.

490*c*. The foregoing cut illustrates the analysis sheet used to show the cumulative cost of the various items entering into the general expense account from month to month. These sheets are generally of twenty-four columns, each ruled as shown, and are kept in a binder. Notice that the items entered in the first left-hand column show all details of the charges to the expense account during the month of January. Where there are many items in an account, these details are first ascertained by using an analysis sheet like the one shown in illustration 95. The total, $143.70, should, of course, agree with the balance of the account shown in the trial balance for that month. The next column shows February expenses, column three showing the total for the two months ending February 28, $280.70, which should agree with the general expense balance in the trial balance for February, and so on throughout the year. Note the figures in red in the month of February. They appear as a credit to the account in the ledger for a small sale of carbon paper, and indicate the method of disposing of such items.

Exercises in Preparing Analysis Sheets

The following illustration shows the items appearing in the debit column of a general expense account for three months. Prepare two analysis sheets, one showing the various items separated in groups for one month, similar to illustration 95, and another showing the cumulative results of the account for the three months, similar to illustration 96.

(1) The expense account of Smith & Son shows the following items:

April 1. Coal bill, $16. – – 4. Electric light bill, $9.63. – – 10. Gas bill, $6.15. – – 14. Cleaning office and windows, $3.50. – – 16. Telephone bill, $12.50. – – 17. Telegrams, $1.75. – – 18. Stationery and printing, $3.50. – – 20. Postage, $10. – – 24. Postage, $3.00. – – 27. Stationery, $9.60. – – 30. Cleaning office and windows, $3.50. – – 30. Telegrams, $2.75. – – 30. Rent, $85.

May 2. Gas bill, $6.75. – – 4. Telegrams, $1.30. – – 8. Electric light bill, $11.50. – – 9. Postage, $2.60. – – 12. Telephone, $12.50. – – 18. Stationery and printing, $7.75. – – 19. Long distance telephone charges, $3.20. – – 25. Vehicle license, $6.00. – – 31. Rent, $85.

June 5. Electric light bill, $9.50; gas bill, $3.20. – – 10. Postage, $10 – – 15. Cleaning office, $2.40. – – 17. City directory, $4.00. – – 20. Brooms and janitor's supplies, $3.35. – – 23. Repairing typewriters, $7.50. – – 25. Cleaning rugs and carpets, $8.25. – – 30. Rent, $85.

AMERICAN, OR CONTINENTAL, FORM OF TRADING STATEMENT.

491. The trading and profit and loss statement shown in illustration (97) differs in its arrangement from the report form of the same statement shown in illustration 87, although it is prepared from exactly similar data and for the same purpose. It is variously known as the American, the Continental, and the "technical" form of statement, and is the form usually preferred by accountants.

ILLUSTRATION 97.

Trading and Profit & Loss Statement.
Year ending

DEBITS.		
Merchandise on hand Dec. 31, 19 , per inventories		25 000 00
-add-		
Purchases for year	125,000.00	
Less rebates and allowances	15,000.00	110 000 00
Boxing, packing and shipping		600 00
Warehouse labor and expenses		300 00
		135 900 00
-deduct-		
Merchandise on hand Dec. 31, 19 , per inventories		65 000 00
Cost of merchandise sold		70 900 00
Gross profit on trading		24 800 00
		95 700 00
Administrative expenses -		
Salaries of officers	2,000.00	
Salaries of office help	1,600.00	
Office supplies	600.00	
Postage & stationery	500.00	
Miscellaneous	150.00	4 850 00
Selling expenses -		
Salesmen's salaries	1,000.00	
Salesmen's commissions	1,000.00	
Salesmen's traveling expenses	1,000.00	
Samples, sample cases	1,000.00	
Premiums	500.00	
Advertising	500.00	5 000 00
Rent	1,200.00	
Insurance	400.00	
Taxes	200.00	1 800 00
Bad debts		650 00
Repairs and renewals to buildings		800 00
Net profit		15 740 00
		28 840 00
Disposition of profit -		
Reserve for items in inventory not staples	1,000.00	
Reserve for doubtful accounts	1,000.00	
Reserve for depreciation of buildings	740.00	2 740 00
Interest on Jones' capital 10,000 1 yr. at 6%	600.00	
Interest on Brown's " 20,000 1 yr. at 6%	1,200.00	1 800 00
1/3 profit to Jones' capital a/c	3,733.33	
2/3 " " Brown's " "	7,466.67	11 200 00
		15 740 00

John W. Brown Merchandise Company.
December 31, 19 .

CREDITS.		
Gross sales		100 000 00
Less -		
Rebates & allowances	1,000.00	
Returned sales	1,200.00	
Discounts on sales	2,100.00	4 300 00
Net sales		95 700 00
		95 700 00
Gross profit on trading brought down		24 800 00
Purchase discounts		3 000 00
Sale of old material		400 00
Interest on accounts		100 00
Warehouse rental		500 00
Dividends received on accounts written off as bad		40 00
		28 840 00
Net profit (year's business) brought down		15 740 00
		15 740 00

ILLUSTRATION 98.

Statement of Resources & Liabilities.
Year ending

RESOURCES.			
Cash on hand		100	00
Cash in bank (First National)		2 500	00
Postage on hand		15	00
Mdse - per inventories (at cost)	65,000.00		
Less reserve for items not staples	1,000.00	64 000	00
Notes receivable	6,000.00		
Accrued interest on notes	30.00	6 030	00
Accounts receivable			
Due in 30 days	15,000.00		
Due in 60 days	15,000.00		
Past due (Good)	2,000.00		
Past due (Doubtful)	1,400.00		
Total	33,400.00		
Less reserve for doubtful accounts	1,000.00	32 400	00
Accrued warehouse rental		100	00
Total current resources		95 145	00
Supplies on hand - per inventories		1 200	00
Unexpired insurance premiums		1 450	00
Advances to agents		340	00
Property & equipment			
Furniture & fixtures	700.00		
Delivery equipment	1,600.00		
Real estate	10,000.00		
Buildings (subject to mortgage per contra)	14,800.00		
Total	27,100.00		
Less reserve for depreciation on bldg.	740.00	26 360	00
Total resources		124 495	00

John W. Brown Merchandise Company.

December 31, 19 .

LIABILITIES.			
Overdraft - Second Nat'l Bank		340	00
Notes payable - bank loans	30,000.00		
Notes payable - mdse. notes	15,000.00	45 000	00
Accrued interest on notes & mtg.		355	00
Accrued commission		1 000	00
Accrued taxes		300	00
Accounts payable		26 500	00
Total current liabilities		73 495	00
Mortgage payable (on building per contra)		8 000	00
Total liabilities		81 495	00
J. Jones - Investment	10,000.00		
Add interest on capital	600.00		
Add 1/3 net profit	3,733.33	14 333	33
B. Brown - Investment	20,000.00		
Add interest on capital	1,200.00		
Add 2/3 net profit	7,466.67	28 666	67
Total liabilities & capital		124 495	00

While the amounts differ, and there are several items included in illustration 97 which are not found in illustration 87, a careful comparison will reveal the similarity between the statements. The principal differences are noted in the following paragraph.

491*a*. The principal differences are as follows:

(1) The *debits* appear on one side and the *credits* on the other side of the statement 97, corresponding with the two sides of an account, instead of the debits appearing under the credits as shown in illustration 87.

(2) In illustration 97, sales discounts are considered *as decreasing returns from sales* (¶226*a*, ¶231*a*), while purchase discounts are considered as showing *an income derived from having the capital available to prepay bills.* (220*b*, ¶225*b*)

(3) Observe that several credit items are shown in the profit and loss section which are not shown in illustration 87, such as "Sales of old material," "Interest on accounts," "Warehouse rental," "Dividends received," etc.

(4) Note that in the disposition of the net profit, *reserves* are set apart for *depreciation in the inventory,* for *doubtful accounts* and for *depreciation of buildings.*

(5) Note also that deductions for the interest on each partner's capital are made before the division of profits between the partners is made.

492. The statement of resources and liabilities shown in illustration 98 is similarly known as the American, the Continental, or "analytical" form of that statement. It contains results that are exactly similar to those as shown in the statement of resources and liabilities in illustration 93. Like the statement shown in illustration 97, this form is preferred by accountants.

EXPLANATION OF OTHER ACCOUNTS.

493. In addition to the accounts explained in the preceding pages, there are many others required in various lines of business. A number of these accounts are explained in more or less detail in this chapter.

SHIPMENTS AND CONSIGNMENTS.

494. Goods are frequently shipped by one person to another to be sold "on commission" by the second party, who acts as the representative or *agent* of the first party.

495. The party making the shipment is known as the *consignor*, and he keeps a record of the shipment in an account known as a "shipment" account.

496. The party receiving the shipment is known as the *consignee,* and he keeps an account of the goods received under the name of "consignment" account. The consignee does not *purchase* the goods; they still belong to the consignor. When the goods are shipped, they are accompanied by an "invoice of shipment." (¶588.)

497. After the consignee sells the goods, he deducts a certain percentage on the total sales as payment for his services, which is known as his *commission*, and also for any other charges which may have been incurred in effecting the sale of the goods. The remainder, which is known as the "net proceeds," belongs to the consignor.

498. According to the laws of agency, the consignee becomes indebted to the consignor for the net proceeds of the goods as soon as they have been sold, hence the net proceeds should be remitted or credited at once to the consignor by the consignee.

499. A statement known as an "account sales" is rendered by the consignee to the consignor, showing in detail, (1) the sales, (2) the charges, and (3) the net proceeds. An account sales may be rendered when the goods are but partly sold, if so desired. (¶589)

500. The object of shipment accounts is to record our dealings with "agents" or "commission merchants" to whom we ship goods for sale on commission,—that is, for sale for our account and at our risk.

501. The object of consignment accounts is to record our dealings with those who ship goods to us to be sold for their account and at their risk.

502. Shipment and consignment accounts as they are shown in this chapter are intended to familiarize the student with the principles of debit and credit involved and to show the manner in which a few shipment and consignment accounts may be kept in the books of an ordinary mercantile business. They are not intended to illustrate the best methods of keeping these accounts in a regular shipping or commission business, which will be fully illustrated and explained in the special commission set accompanying this work.

SHIPMENT ACCOUNTS.

503. The record of a shipment is kept in the books of the consignor under the title of "Shipment."

504. There are two general methods of keeping shipment accounts. One is to open a separate account for each shipment, adding the name of the party to whom the shipment is made, for instance, "Shipment to Wm. F. Day & Sons, Chicago." Where more than one shipment is made to the same party, they may be numbered as No. 1, No. 2, etc. Another method is to open a general "goods on consignment" account, to which all the items relating to the various shipments are credited and debited, with a separate account with each shipment entered as a memorandum account in a special book kept for that purpose. The last method does not differ from the first method, except that it shows in one account the same results that would be shown in a number of accounts under the first method.

505. The object is to ascertain the *amount gained or lost* on our different shipments of goods to others for sale on commission. When account sales are received for but part of the goods shipped, in closing the shipment account those remaining

unsold in the hands of the consignee are treated as an inventory balance, under the designation "Goods on consignment," exactly as in a merchandise account, until an account sales for the remainder of the shipment is received.

506. When goods are shipped on consignment, they are usually entered by the shipper on the invoice of shipment at *cost price*, although sometimes the market or selling price is given. Not infrequently in such lines of business as those conducted by stockmen, dairymen, fruit growers and gardeners, where the cost price of the goods shipped is not definitely known, no prices whatever are given on the invoice of shipment. Full details of the practices common among shippers and commission merchants are given in the commission set accompanying this work.

506*a*. It is not unusual, particularly when only occasional shipments are made, to omit opening a separate ledger account for them. Instead a memorandum record of each shipment is made in a separate shipment book kept for that purpose. The record is a practical reproduction of the invoice of shipment. When the account sales is received the proceeds are credited to sales account, the same as a regular sale. At the same time a record of the proceeds is entered in the shipment book, which will then show the shipment closed. The loss or gain on each shipment can be ascertained, if desired. When this method is followed, the value of the goods for which account sales have not been received must be added to the inventory at the time of closing the books, being designated as "goods on consignment." This method is not recommended, as it is liable to lead to confusion and inaccuracies in the trading statement.

Rule for Debiting and Crediting Shipment Accounts.

507. *Debit shipment accounts for costs: credit for returns.*

507*a*. Debit the shipment, under an appropriate title, for all *costs*.

507*b*. Credit the shipment, under an appropriate title, for all *returns*.

508. The various applications of the rule are as follows:

509. Debit shipments,—

a. For the invoice (generally the cost) value of the goods shipped.

b. For all charges, such as drayage, insurance, freight prepaid, etc.

c. For drafts drawn on us or for cash advanced by us on account of the shipment.

510. Credit shipments,—

d. For all drafts drawn by us or other *advances* made to us on account of the shipment.

e. For all returns (proceeds) when account sales are received.

f. For all goods returned for which the shipment had been previously debited.

g. For insurance received on goods damaged or destroyed.

511. Observe that in every instance the account is debited for the *cost* of anything of value relating to the shipment.

512. Observe that in every instance the account is credited for the *returns* from anything of value relating to the shipment.

513. It will be observed that a shipment account is similar to a personal account in many respects. It is debited when the agent is the *receiver* of anything of value from us and is credited when he is the *giver* of anything of value to us. The difference between the two sides of the account, however, shows a *loss* or a *gain* to us, instead of a resource or liability as in a personal account.

514. *Acting on the principle* that the consignee is responsible for all goods consigned to him until an account sales has been received or a settlement made, many bookkeepers follow the practice of charging the personal account of the consignee with the value of the shipment and charges until an account sales with returns is received, when the personal account of the consignee is credited to close, with the difference transferred to the profit and loss account or to a separate account under an appropriate title, such as "Shipment Gains & Losses." For occasional shipments this method is approved.

To Close Shipment Account.

515. The difference between the two sides of a shipment account, before an account sales has been received and returns (proceeds) credited, will show a balance which is a resource; after an account sales has been received for all the goods shipped and the proceeds credited to the account, the difference will show a *gain* or a *loss*—a gain if the credit side is the larger, a loss if the debit side is the larger.

516. If an account sales is received before all the goods are sold, and the shipment account is credited for the returns (proceeds) shown by the account sales for that portion of the goods which has been sold, the difference between the two sides of the account, *after the account is credited "by inventory" for the value of the goods remaining unsold* in the hands of the consignee, will show the gain or the loss on the goods sold and reported in the account sales. The inventory is considered as a *sundry resource inventory* described in ¶468*a*, the shipment account being credited for the amount.

517. To close. After the trading statement has been prepared, shipment accounts are closed by a journal entry made up from the trading statement. When the closing item for any shipment account has been posted, which should balance the account, rule the closing lines in red ink and enter the footings in black ink.

CONSIGNMENT ACCOUNTS.

518. Consignment accounts (or "commission sales" as they are called by most commission merchants) differ in several important particulars from shipment

accounts. When an agent receives goods to sell on commission, he does not in any sense buy them, and when he expends money upon them in paying the freight, drayage or other charges, and debits the consignment, he does so, it is true, with the idea that the property received is "good for it," and with the expectation that he will get his money back from the proceeds of sales, but nevertheless with a knowledge of the fact that the consignor (shipper) is personally responsible to him (the agent) for all such expenditures and also his charges (commission, etc.) for selling. On the other hand, the consignor looks to the consignee (agent) as being personally responsible to him for the proper care of the goods while in his possession, as well as for any proceeds that the shipment may return to him.

519. A change takes place, however, in the relations existing between the consignee and the consignor *the moment the goods are sold.* Prior to that time the consignee is not responsible for the value of the goods, nor could he be held responsible for any loss that might occur so long as he exercises ordinary diligence in their care; but the moment the goods are sold, the consignee becomes directly indebted and is personally responsible to the consignor for the value of the goods sold after his charges have been deducted. Even if he sells the goods on credit and the party to whom he sells should fail, he is still held responsible to the consignor. He may, however, deduct a certain percentage for taking such risk, unless the consignor instructed him to sell for cash only.

520. Consignment accounts, therefore, in reality closely resemble personal accounts (¶513). When the consignment is debited, the consignor would be debited if he received the value direct from the consignee, and when the consignment is credited, the consignor would be credited if he gave the consignee the value direct. *The consignment account, therefore, represents the consignor.*

521. Consignment accounts are not debited for the value of the goods received but only (*a*) for outlays made on account of consignments, such as freight, drayage, advances, etc., (*b*) when account sales are rendered for commissions, or other charges deducted, and (*c*) for the net proceeds. The account is credited for all sales.

522. Consignment accounts are kept under a designating title, such as "O. B. Wharton's Consignment, Columbus, O." and if different consignments are received from the same party, they should be numbered consecutively. In commission houses it is usually the custom to number all consignments in the order received and thereafter to refer to each consignment by number.

522*a*. Those who make a specialty of selling goods on commission are known as "commission merchants". When they sell stocks, bonds and other securities, they are called "brokers."

Rule for Debiting and Crediting Consignment Accounts.

523. *Debit consignment accounts for costs: credit for returns.*

523*a*. Debit the consignment, under an appropriate title for all *costs*.

523*b*. Credit the consignment, under an appropriate title, for all *returns*.

524. The various applications of the rule are as follows:

525. Debit consignments,—

a. *At the time received*, for all charges paid such as freight, drayage, etc.

b. *When on hand*, for all charges for cooperage, boxing, bagging, repacking, advertising, or other outlays necessary for the preservation of or for effecting the sale of the goods.

c. For all goods returned to us after having been sold and credited to the consignment, and for shortage, damage or overcharge claims allowed on goods previously sold.

d. For all drafts accepted or paid, or for other advances made on account of the consignment.

e. *When account sales are rendered*, for our charges, such as commission, insurance, storage, guarantee, etc.

f. For the consignor's *proceeds* remitted with the account sales or credited to his personal account.

526. Credit consignments,—

g. For all sales of goods belonging to them.

h. For all rebates for overcharges on freight, drayage, etc., or for other charges rebated, previously debited to the account.

i. *When the charges exceed the total sales*, for the amount to close the account (owed by the consignor).

527. **Observe** that in every instance the account is debited for the *cost* to the consignor of all outlays, advances, etc., made on account of the consignment by the consignee, and for his charges and for the proceeds remitted or credited to the consignor.

528. **Observe** that in every instance the account is credited for the *returns* from sales, allowances, etc., received by the consignee for the account of the consignment.

529. In a regular commission business, consignment accounts are kept in special books and, therefore, do not appear separately in the ledger. In some systems of commission accounting, controlling accounts are kept in the general ledger. The latest and best methods in commission accounting are fully explained in the regular commission set accompanying this text.

To Close Consignment Accounts.

530. The object is to ascertain the amount of the consignor's *proceeds* and the consignee's *compensation*, such as commissions, storage, guarantee, etc.

531. Before closing it is customary (1) to prepare the account sales, (2) then to make the proper entries for the charges, etc., and for the net proceeds, after which the proceeds are remitted or credited to the consignor.

532. To prepare the account sales. From the consignment account it is customary to make out the account-sales as follows: (*a*) fill out the heading of the account-sales; (*b*) from the credit side of the consignment account enter the amount of sales, referring, if necessary, to the books of original entry for the items; (*c*) from the debit side of the account enter the amount of the charges already paid; (*d*) calculate and enter on the account-sales the charges for commission, insurance, storage, guarantee, etc.; (*e*) deduct the total charges from the total sales, which will give the proceeds belonging to the consignor.

533. To close. When the account sales has been prepared, it will be observed that the entries for the sales and for the freight and other charges already paid (¶525 *a*, *b*, *c*) have been made in the books, and the only entries that remain to be made are for the *commission and other charges*, and for the *proceeds*, which are not determined until the account sales is prepared. Therefore, to close the account, make the proper entry for the charges not yet entered, and for the proceeds if they are to be credited to the consignor's account. If the proceeds are to be remitted, write the check or note or other paper for the proper amount and make the proper entries for the same. When these are posted, the consignment account should balance, when the proper closing lines and footings should be entered.

COMMISSION ACCOUNT.

534. Commission is a percentage charged by commission merchants, agents, or brokers for services in buying and selling merchandise, real estate, stocks, bonds, mortgages, insurance, or other forms of property. This account is, therefore, a *service* account. It is debited for the *cost* of all commission services *received* (which we pay for) and credited for the *returns* from all commission services *given*. When commissions from various sources are to be shown separately in the profit and loss statement, they may be classified to whatever extent desired by distributing them on an analysis sheet.

Rule for Debiting and Crediting Commission Accounts.

535. *Debit commission accounts for costs: credit for returns.*

536. Debit commission account, under the proper heading,—

a. For the value of all commission services earned and unpaid, owed to us by others at the beginning of business.

b. For the value of commission services received from others and paid for by us or credited to them.

537. Credit commission account, under the proper heading,—

c. For the value of all commission services earned and unpaid, owed to others by us at the beginning of business.

d. For the value of commission services given to others for which they pay us or we debit them.

538. **Observe** that in every instance the account is debited for the *cost* of commission services received.

539. **Observe** that in every instance the account is credited for the *returns* from commission services given.

540. **The difference** between the two sides of a commission account shows a *loss* when the debit side is the larger and a *gain* when the credit side is the larger.

541. **To close.** After the profit and loss statement has been prepared, commission accounts are closed by a journal entry made up from the profit and loss statement. When the closing item to a commission account has been posted, which should balance the account, rule the closing lines in red ink, and enter the footings in black ink.

BRANCH STORE ACCOUNTS.

541. **When one or more branch stores are conducted,** either in the same or other cities, accounts with each of them should be kept in the ledger of the main store. Several methods of keeping such accounts are in common use. Two of the simplest and most practical are here explained, one being an amplification of the other.

541*a*. **First method.** This method involves the opening of but one account with the branch store. This account is opened under a title that designates the location of the store, as "Market Street Store," or if in another city, "Omaha Store—96 Main St." The account is debited for everything furnished by the main store or for account of the main store, i.e., for all *costs* of the branch store; and it is credited for all returns to the main store of cash, notes, or any other value sent in for credit from the branch store. The account is treated exactly the same as a merchandise account, except that at closing, the *total net resources* of the branch store must be included as an inventory. A single account may be kept, or separate accounts—one for costs and the other for returns—may be kept. All bills of goods intended for the branch store should be returned to the main store, after having been checked, found correct, and entered in the books of the branch store.

Second method. This method is exactly similar in principle to the method already described, except that separate accounts are kept in the books of the main store for the various items represented in the costs and returns of the branch store, which are exactly similar to the accounts kept for the same costs and returns of the main store.

Rule for Debiting and Crediting Branch Store Accounts.

542. *Debit branch store accounts for costs: credit for returns.*

543. Debit the branch store, under its proper title, or sub-title, in the books of the main store,—

a. For all goods or money furnished it from the main store.

b. For all goods bought for it or by it for account of main store and sent direct to the branch store.

c. For all outlays for furniture, fixtures, delivery equipment, salaries, rents, taxes, drayage, or other investments or expenses on account of the branch store.

544. Credit the branch store, under its proper title or sub-title, in the books of the main store,—

d. For all cash, notes, acceptances, accounts, etc., returned to the main store, and for all cash deposited in bank to the credit of the main store.

e. For all goods sold, as shown by reports of sales, when a separate account for sales is kept.

f. For all merchandise or other property returned to the main store after it has been charged to the branch store.

g. For all returns from any investment, expense or other account turned into the main store.

545. When separate principal and subsidiary trading accounts are kept for the branch store in the books of the main store, the items indicated in ¶543*a* and ¶544*d* correspond with the debit and credit items of an ordinary personal account. Items included in ¶543*b* and ¶544*e-f* correspond with the ordinary purchase, sales and subsidiary trading accounts and items indicated in ¶543*c*, and ¶544*g* correspond to similar items appearing in the usual investment, expense and income accounts.

545*a*. When the second method is used, the inventories are distributed to the various accounts which they affect in the preparation of the trading statement at the closing of the ledger.

545*b*. When branch stores are located at a considerable distance from the main store, as a matter of convenience the cash received is sometimes deposited in a nearby bank other than the one in which the account with the main store is kept. When such is the case, it is deposited in the name of the owner and is subject to his check. This does not in any way affect the manner of keeping the accounts except that a different check book and bank book, are kept and when cash is balanced the balance in this bank must be added to the balance in the regular bank of the concern.

545*c*. The books in the branch store are kept exactly like the books of any other store except that the *main store account* represents the owner's interest and should be kept in the same way. Its title should be the same as that representing the ownership in the main store. The main store account should be credited for the net gain or debited for the net loss at the time of closing the books.

545*d*. *From this it will be seen that* the branch store has no accounts with the parties from whom goods are bought, whether shipped direct to the branch store or not. After seeing that the bills are correct, they are turned over to the main store, first making the proper entries for the same in the books of the branch store, crediting the main store.

545*e*. Branch stores are required to make daily, weekly, or monthly statements showing purchases, sales, receipts, payments, expenses, incomes, etc., and at stated times complete trading and profit and loss statements, and statements of resource and liabilities are sent in, which are checked against the accounts of the main store, and from which adjusting entries are made.

To Close Branch Store Accounts.

546. The object is to show the profit or the loss derived from conducting the branch store.

547. The inventories relating to branch store accounts consist of an inventory of the *total resources* of the branch store, which includes not only the merchandise, but also furniture and fixtures, cash on hand, personal accounts receivable, notes receivable or any other thing of value, as shown by the statement of resources and liabilitites taken from the books of the branch store, and an inventory of the total *liabilities*, if any, of the branch store, as shown by the same statement. After these inventories are disposed of, as instructed in ¶464 to 474*c*, the difference between the two sides of the branch store account will show a net gain or loss—a gain if the credit side is the larger, a loss if the debit side is the larger. This net gain or loss should appear as an item in the trading statement of the main store.

548. To close. After the trading statement has been prepared, this account is closed by a journal entry made up from the items appearing in the trading statement. When the closing item for this account has been posted, which should balance it, then rule the closing lines in red ink and enter the footings in black ink, as shown in other similar accounts.

BRIEFER EXPLANATIONS OF ACCOUNTS.

549. Stocks and bonds. A general account may be kept under this title, or a separate account may be kept with each kind of stocks or bonds purchased, such as "Penna. R. R. Stock," or "U. S. Bonds." The account is debited for all *costs* and credited for all *returns*, and is kept exactly like *property investment accounts* (¶376), a separate *expense and income* account being kept for any outlays or returns in the shape of taxes, dividends, interest, etc.

549*a*. Stocks and bonds are inventoried at *cost price*, or at *market price when less than cost price*. If it is desired to carry stock or bonds at cost on the ledger, if the market price is less than the cost price, a reserve account may be opened, which should be credited for the amount of the depreciation at the time of closing the books. The expense and income account belongs to the profit and loss statement.

550. Sundry debtors and sundry creditors accounts. "Sundry Debtors" is a title under which accounts with transient or irregular customers are entered, the purpose being to avoid the necessity of opening a separate account with each person. When a sale is made to a transient customer, sundry debtors' account is debited for the amount, the name of the party being written *in the explanation column*. When payment is received, the party is credited for the amount *on the same line* on the credit side of the account. The *difference* between the two sides of the account shows the amount owed to us by others and is, therefore, a *resource*, which should be included in the list of accounts receivable in the statement of resources and liabilities.

ILLUSTRATION 99.

Sundry Debtors

19 May	10	Wm. Beech		7	25	19 May	20	Cash	7 25
	12	John & Henry		3	16				
	17	Billings & Co		6	38		23	Cash	6 38
	21	C. F. Knox			85				

550*a*. *Sundry creditors'* account is kept in the same manner as the sundry debtors' account, the only difference being that sundry creditors' account is first credited, and is then debited on the line opposite when the credit item is paid. The *difference* shows a liability, and this account should be included in the list of accounts payable.

551. Executors and administrators' accounts. It is frequently necessary for business men to take charge of the settlement of estates. To avoid the necessity of keeping a separate set of books, the necessary accounts are sometimes carried in the books of their business, although this practice is not commended, on the principle that such accounts should not be mixed with the regular accounts of a business. In some states it is prohibited by law. When this plan is followed, however, a general account with the estate should be kept under the name of the estate, as, "Estate of Henry Wilson," which is debited and credited like an owner's account. It is credited for all the assets of the estate and debited for all the liabilities. Separate accounts for these assets and liabilities should be opened under appropriate titles. Separate personal accounts should be kept with each heir or legatee, which should be charged for all money paid to them on account of the estate. When it is desired to make a report of the affairs of the estate prior to or at the time of its final settlement, the accounts belonging to the estate should be made up in a separate statement, any profits or losses belonging to the estate being closed in the usual way into the general account of the estate.

551*a*. *When closing the books of a business which includes executors or administrators' accounts,* these accounts should not appear in the statement of resources and liabilities of the business, but the difference between the total debits and the total credits of these accounts should be shown in a single item in the statement of resources and liabilities as a personal resource or liability of the executor or administrator of the estate, this being necessary in order to maintain an equilibrium of debits and credits in the trial balance.

551*b*. *In recent years* the trust companies of the country have been acting in the capacity of executors and administrators for estates, and have largely superseded individuals. Their methods of keeping such accounts are similar in principle to those already described.

552. Leasehold account. This is an account which is opened when a lease covering a term of years is purchased. The value of the lease, therefore, is reduced each year, as it expires, in proportion to the number of years it has to run. This account is treated in every respect like an insurance account (¶325), the monthly, quarterly or annual expired value of the lease being credited to the leasehold account and debited to leasehold expense, rent, or general expense. It is a resource account, and should be included in the statement of resources and liabilities.

553. Collection and exchange is an account which is kept to show the cost of making collections through banks, collection agencies, etc. It is debited for the cost of making collections from others and credited for any returns for like service rendered to others. It is seldom kept as a separate account except in banks, as

such items are usually charged to general expense, although a separate account may be kept where there is a sufficient number of items to justify. It is a *service* account and should be included in the profit and loss statement.

554. Good-will account. The good-will of a business is frequently considered valuable and may be bought and sold in the transfer of the business into new hands. Good-will is the value placed upon the disposition or inclination of the people to patronize a particular business, owing to the reputation it has already established.

554*a*. *When the purchaser is a corporation* and the bill of sale covers a specified amount to be paid for good-will, for which that account is debited when opened, the rule is to let it stand without change at the close of subsequent fiscal periods, as the amount does not mean anything except to show what the good-will cost in the first instance. The practice is not unusual, where sufficient profits are being made, to write off against profits a certain percentage of the amount charged to good-will account; but it should not be overlooked that this practice, unless it be to correct an actual shrinkage in the value of the good-will since the date it was acquired is, in a sense setting aside a secret reserve, which is condemned by some authorities. However, if a special reserve for that specified purpose is set up so that the entire transaction is shown in the statements of the company, it would seem that no valid objection to this practice could be sustained.

554*b*. *When the purchaser is an individual or a firm*, the account is usually credited at the close of each fiscal period for such proportion of the amount debited as may be determined upon by the owners, which should be charged to profit and loss and should appear as a separate item in the profit and loss statement.

554*c*. *The difference* shown by a good-will account is considered as a fixed resource (asset), since its value is fixed and it cannot be used as working capital. Good-will is taxable in some states. It should appear in the statement of resources and liabilities. If treated as indicated in ¶554*b*, the account will eventually disappear; and it is generally preferred by business men that it should be wiped off the books as soon as possible, certainly as soon as the good-will of the old concern can fairly be considered as being merged into the new concern.

555. C. O. D. accounts. Where goods are sold C. O. D. (collect on delivery), various methods are followed. With some it is the custom to charge the express company with the amount of the bill instead of the party to whom the goods are shipped, because the express company is responsible either for the return of the money or of the goods. When this method is followed the name of the express company should be followed by the letters "C. O. D." *Another method* is to debit the account of the party to whom the goods are shipped, writing the letters "C. O. D." in connection with the charge made and in the explanation column of the account in the ledger. In any event, the account is treated the same as a personal account, the difference showing a debit balance, which is a resource that should be included in the statement of resources and liabilities.

556. Agents' accounts. The method of keeping these accounts varies, depending upon the contract made with the agent. In case his duties are limited to those of a salesman or "drummer," his account is not different from an ordinary personal account, being debited for all cash or goods advanced to him and credited for the amount of his expenses as per his expense bills, and also for his salary or commission at stated intervals. In this case the account shows what he owes or what is owed to him, and the balance is, therefore, a resource or a liability. If, however, he acts as a resident agent in another city and goods are shipped in his care, it is the best practice to open a separate account for the goods, which is in every way kept and closed like a shipment account, as described in ¶503, ¶515, etc.

557. Reserve, surplus and undivided profits accounts. These are accounts which are usually opened in the books of stock companies or corporations to show the amount of the annual profits which have been retained in the working capital of the business for special purposes and not distributed among the stockholders. (¶450 to ¶453). Such accounts usually show credit balances.

557*a*. *Reserve account*, setting apart a sufficient amount of the profits to meet any contingent expense or loss of the business, may be opened to offset charges against profits, such as bad debts, depreciation, etc. A reserve account is credited *for the amount of the profits set apart for the particular purpose indicated in the title of the account.* It is debited for such sums as are necessary to meet the purpose for which the profits were reserved.

557*b*. *Surplus and undivided profits* are practically synonymous accounts, both showing profits belonging to the owners which have not been distributed. Surplus account, however, is generally understood to represent that part of the profits which has been set apart as a permanent addition to the working capital. Undivided profits account generally represents that part of the net profits which is "left over" after the different sums for the various reserve, dividend, surplus and other accounts have been set apart and deducted. Surplus and undivided profits accounts are credited for the amounts of the profits set apart for the purpose indicated in the title of the account. They are debited when the purposes for which they were opened have been accomplished.

557*c*. *The difference* shown by a reserve, surplus or undivided profits account always appears as a credit balance, representing the unused or available value of the particular reserve, surplus, etc., indicated in the title of the account. When reserve accounts are set up for a special purpose, such as reserves for depreciation of property or other resources, for doubtful accounts, etc., such reserves should be deducted from the book value of those accounts on the statement of resources and liabilities, the net amount being extended as the actual resource. This method is required by banks where financial statements are prepared with the object of securing loans. Balances shown by surplus, undivided profits and other similar accounts which are general in character, are classed as *secondary liabilities* of the concern, and as such should appear as separate items in the section of the statement of resources and liabilities (¶488*b*) representing the ownership of the business. Observe, however, that such accounts as "Reserve for Depreciation," "Reserve for Doubtful

Accounts," or other accounts which are specific in their character, are not classed as liabilities but as *offsets against resources* (assets) and should be deducted from the corresponding resource account in the statement of resources and liabilities. A *fund* reserve account that offsets a fund account is more in the nature of a *responsibility* than a liability.

557*d.* *Reserve* accounts, as described in the preceding paragraphs (¶557, etc.) must not be confused with *fund* accounts, which represent funds that are actually taken from the working capital in cash and set apart to create sinking, redemption and other funds, as described in ¶558. The distinction is clearly shown when we say:

Sinking fund Redemption fund Interest fund	as *contra* to	Sinking fund reserve Redemption fund reserve Interest fund reserve

558. Sinking and redemption funds, etc. "A fund" may be created for a number of purposes, among them, (1) to liquidate a known existing liability, such as bonded indebtedness, (2) to provide an available or quick asset to meet a specific future obligation, such as plant renewal or betterment, and (3) to provide against any embarrassing contingency or unexpected losses. These funds are usually taken out of the cash assets of the business, and may be deposited in a separate bank account or converted into interest-bearing securities or other form of property which will earn an income, or they may be transferred to a trustee or other agent who shall invest them in such securities or make such disposition of them as is required by the agreement with the trustee or agent. *Two classes of accounts are required* for the proper record of such funds, one class representing the profits set apart for the creation of these funds, which are known as *fund reserve* accounts. These accounts are similar to those described in ¶557*a*, except that they include in their titles the name of the corresponding *fund* account to which they belong. The other class shows the investment or disposition of these funds (the actual cash or equivalent) which are known as *sinking* or *redemption fund* accounts, of which several accounts may be required to show the transactions in relation to a single sinking or redemption fund. In large corporations a separate set of books is usually kept to contain the sinking fund accounts. In both classes of accounts, the identity of the fund to which such accounts belong should be indicated in the title, such as "Sinking Fund Reserve," "Redemption Fund Reserve," "Bonds in Sinking Fund," "Sinking Fund Trustee," etc. It should be remembered that the *reserve* accounts show the amount of the profits that has been set apart *for the creation of the fund,* while the *fund* accounts show *the investment or disposition that has been made of the fund;* consequently, they are *contra* accounts, one offsetting the other in purpose, although they may differ in the amounts shown in each account at a given time. Hence, reserve accounts usually show *credit* balances, while fund accounts usually show *debit* balances.

Rules for Debiting and Crediting Fund Reserve Accounts.

558*a*. Debit fund reserve accounts,—

1. For premiums on investments when it is desired to carry the investments at par.
2. For losses incurred in connection with realizing on securities.
3. For taxes on the investments or incomes therefrom, in states where they are taxable.
4. For expenses incurred in making investments.
5. For amount "to close" when the reserve has served its purpose.

558*b*. Credit fund reserve accounts,—

1. For all amounts set apart from profits to create the reserve named in the title.
2. For interest received on bonds purchased for and belonging to the fund.
3. For dividends received on stocks purchased for and belonging to the fund.
4. For interest received on mortgages (if any) belonging to the fund.
5. For interest received on current bank balance in the fund.
6. For profits on sales of any securities belonging to the fund.
7. For discount on bonds or stocks when it is desired to carry them at par in the fund.
8. For accrued income on sinking fund investments at time of closing books.

558*c*. The items for each sinking, redemption, or other fund, may be kept in a single account, but they are usually separated into three accounts, one for the *cash* belonging to the fund, another for the *investments* belonging to the fund, and a third for *accruals*. The titles of these accounts for a sinking fund would be, "Sinking Fund Cash," "Sinking Fund Investments," "Sinking Fund Accruals."

Rules for Debiting and Crediting the Various Fund Accounts.

558*d*. Debit fund cash accounts,—

1. For all periodical payments of cash to this fund.
2. For all incomes received from investments belonging to the fund, as (*a*) interest on bonds, (*b*) interest on bank balances, (*c*) dividends on stock, etc.
3. For profits on sales of securities in fund.
4. For cash received from sale of investment securities.
5. For cash received from accruals collected.

558*e*. Credit fund cash accounts,—

1. For all investments made from fund, paid in cash.
2. For premiums paid on investments.
3. For expenses paid in making investments.
4. For all cash paid from this fund in liquidating the liabilities for which it was created.
5. For any other payments made from the fund.
6. For the amount "to close" when the fund has served its purpose.

558*f*. Debit fund investment accounts,—

1. For cost of all securities purchased (generally at par.)

558*g*. Credit fund investment accounts,—

1. For returns from all securities sold, at the amount for which they were carried in the fund (generally at par.)

558*h*. Debit fund accrual accounts,—

1. For all payments due the fund at the time of closing books.
2. For all accrued income at time of closing the books.

558*i*. Credit fund accrual accounts,—

1. For cash received for anything previously debited.

558*j*. The three accounts explained in the preceding paragraph may be combined in a single account when the fund is small, although in any case it is better to open separate accounts as required. Investments may be carried in the investment account either at *cost* or at *par value*.

558*k*. *All balances* shown by fund reserve accounts represent what may be classed as *secondary liabilities*, similar to surplus and undivided profits accounts, and should appear *contra* to the corresponding sinking or redemption fund accounts, which show *resources* in the statement of resources and liabilities. The sinking fund accounts show *real assets*, while the reserve accounts show *secondary liabilities* in the sense that when the balances represented are released or transferred from these accounts, they will go back into the surplus or undivided profits account, and will then be available for distribution among the owners of the business, or for other purposes.

558*l*. Accounts relating to sinking and redemption funds, and the corresponding reserve accounts, admit of a great variety of treatment, depending upon the conditions under which the funds are created.

559. Bonus accounts. Frequently in organizing the affairs of corporations it is necessary to offer a bonus to secure the services of promoters, effect sales of stock, or secure a franchise or a charter. In such cases a bonus account is opened, which is debited for the value of all such bonuses allowed. This account is similar to good-will and leasehold accounts. A certain proportion of the amount charged to the account should be closed off into profit and loss at the close of each fiscal period, until the account is finally wiped out and closed.

560. Patent and copyright accounts. These accounts are kept under two conditions.

(1) *When a patent or copyright is purchased*, the account, under an appropriate title, is debited for the cost of the patent or copyright. When all or any part of the patent or copyright is sold or otherwise disposed of, the account is credited at the cost value of what is sold, *i.e.*, for the original price charged to the account. It must be remembered, however, that both patents and copyrights eventually expire as determined by law, and that, consequently, their value is decreased year by year. The account should, therefore, be credited annually for the proportionate part of the cost which has been eliminated by the passage of time. The amount of such decrease, when credited to the investment account, is debited to the income account, or to a separate account, or, in the absence of these, to profit and loss account. Preferably, such amounts should appear as separate items in the profit and loss statement.

(2) When only the *right* or *privilege* is secured to manufacture or sell an article under a copyright or a patent upon payment of a percentage or royalty, the account is kept for the purpose of showing the cost of the royalties paid. This cost is, therefore, a part of the cost of the article manufactured or sold, and, consequently, prop-

erly belongs to the trading statement. A separate account may be kept under an appropriate title, or the royalties paid may be charged directly to the principal account showing the cost of the goods manufactured or sold.

561. Dividend account. This is an account opened in the books of corporations and stock companies when profits are to be divided among the stockholders. A separate account is generally opened for each dividend declared, as "Dividend No. 1," "Dividend No. 2," and is kept for the purpose of showing the amount of each dividend declared and also to show the amount of the different dividends that have been paid to stockholders.

561*a*. *When the dividend is declared,* the account is credited for the amount. As each stockholder is paid his share of the dividend, the account is debited for that amount, so that when the dividends owing to all stockholders are paid in full the account should balance. If at the close of a fiscal period all dividends declared have not been paid, the difference shows the amount due to stockholders and is, therefore, a liability, which should appear in the ownership section of the statement of resources and liabilities.

562. Plant account. This is a general title that is not infrequently used in manufacturing concerns to include the cost of machinery, implements, and other property, excepting real estate, used in the manufacture of goods or articles produced, although it is the better practice to open separate accounts for each. Plant account is an investment account which is debited and credited exactly as real estate investment accounts are debited and credited. Separate accounts should be kept for repairs and renewals and other expenses connected with the maintenance of the property represented in a plant account, for which proper reserve accounts should be set up. This account is sometimes opened under the title of "Machinery" account, or "Machinery and Implements," or "Machinery and Tools."

563. Labor account. This is an account which is usually found in connection with the books of manufacturing concerns. It is *credited* for the total amount of labor performed, as shown by the daily, weekly or monthly pay-roll. The cost of the labor should be charged to the department of the business in which the labor was performed.

563*a*. *The account is debited* for the total amount paid to employees included in the pay-roll, whether in cash or otherwise. The account should balance when all the employees have been paid.

563*b*. *The difference,* if any, shows what is owing to employees and, therefore, is a liability which should appear as a separate item in the statement of resources and liabilities at the close of the fiscal period. A labor account is in reality a con-

densed personal account. However, it should not be included with the ordinary accounts payable, as in most states those who are owed for labor performed are considered as preferred creditors.

564. Franchise account. Public corporations frequently secure valuable franchises and privileges from cities and municipal corporations, sometimes for, and frequently without a consideration. Such franchises are usually of great value to the corporation owning them. When a franchise is purchased, the account is debited for the cost value. If there is no cost value, formal accounts are seldom kept, such franchises being classified as *non-ledger assets*. Under the laws of most states, however, certain limitations are placed upon including the value of franchises in statements of resources and liabilities.

565. Doubtful accounts. Formerly it was the rule to open an account under this heading to show the amount owed to the concern on personal accounts which were considered of doubtful value. This method has been superseded, however, by that of making a list of such accounts at the close of each fiscal period, and then setting up a "Reserve for Doubtful Accounts" account sufficient to meet anticipated losses resulting from doubtful accounts, no entry being made in the personal account of the doubtful debtor until the account is finally considered as uncollectable and of no value, when it is charged against the "Reserve for Doubtful Accounts" account. In the absence of such reserve account, uncollectable accounts should be closed directly into profit and loss account, and their sum should appear as a separate item in the profit and loss statement.

566. Controlling accounts. These are general ledger accounts that are used when separate ledgers are kept for different classes of accounts, such as accounts receivable, accounts payable, depositors' accounts in banks, etc. Each controlling account is kept under a title that indicates the class of accounts included in the separate ledger which it represents. A separate ledger, with its accompanying controlling account in the general ledger, may be kept for any class of accounts which may be classified by the use of special columns in the various books from which the items affecting them are posted. These separate ledgers are sometimes designated as subordinate ledgers.

566*a*. When a controlling account representing a separate ledger is opened in the general ledger, it is debited or credited for the total sum of the balances of the accounts in the ledger it represents. At stated times thereafter, usually at the end of each month, the controlling account is debited and credited for the total of the debit and credit items that have been posted from the different posting books to the accounts in the ledger it represents; for instance, if the total sales for the month charged to accounts in the sales ledger, as shown by the sales book, are

$10,000, at the close of the month "accounts receivable" (the controlling account in the general ledger representing the sales ledger) is debited for that amount, the "sales" account being credited. If the total cash received for the month in payment of accounts contained in the sales ledger is $9,000, accounts receivable account is credited for that amount. It should also be credited with other items, such as discounts, allowances, goods returned, as shown by the footings of special columns in other books relating to customers' accounts. *The difference* between the two sides of the accounts receivable account will then show the sum of the balances shown by the accounts in the sales ledger.

566*b*. To facilitate the work of classifying the items posted to the various subordinate ledgers, and of posting their totals to the controlling accounts in the general ledger, special columns for that purpose should be provided in the cash book, purchase book, sales book, note books, journal, and in any other book used as a posting medium. The items in these special columns are footed and forwarded until the end of the month, when the total amounts are posted to their respective controlling accounts in the general ledger.

566*c*. *To prove the correctness of the balance shown by a controlling account*, the sum of all the balances in the ledger it represents (less any *contra* balances) should equal it. The adding machine can be used advantageously for this purpose. *Contra balances* refer to those that are credit balances in a debit ledger, such as the sales ledger, and to those that are debit balances in a credit ledger, such as a purchase ledger.

BUSINESS PAPERS.

567. These are papers of every description that are used in business, the most important of which are notes, drafts and acceptances, checks, bills, receipts, orders, statements, shipping invoices, account sales, bills of lading, warehouse receipts, letters, vouchers and memoranda of every description. Notes, checks and drafts are generally called commercial paper.

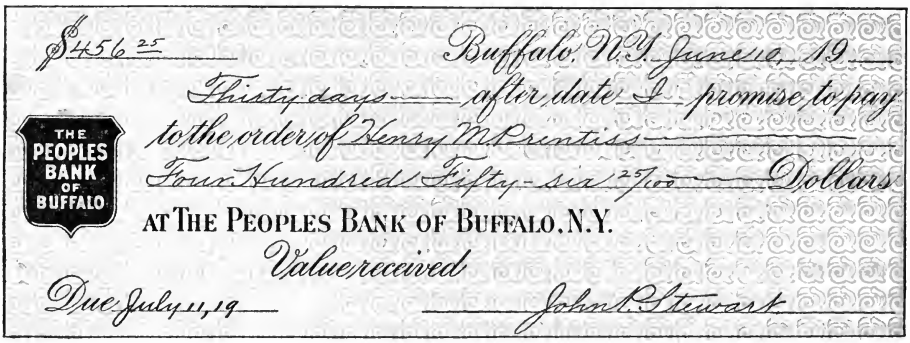
567*a*. *The use of commercial paper* has greatly facilitated and lessened the cost of transacting business. Over 90 per cent of the exchanges of money are effected through the medium of checks, drafts, etc. The charges for exchange between different points, which was formerly quite an item in effecting settlements, have been almost entirely abolished.

568. Written contracts, such as articles of co-partnership, bonds, mortgages, powers of attorney, leases, deeds, certificates of incorporation, insurance policies, licenses, etc., are business papers, but are more properly classed as *legal forms*.

569. A promissory note is an unconditional promise to pay a specified sum of money at a definite future time.

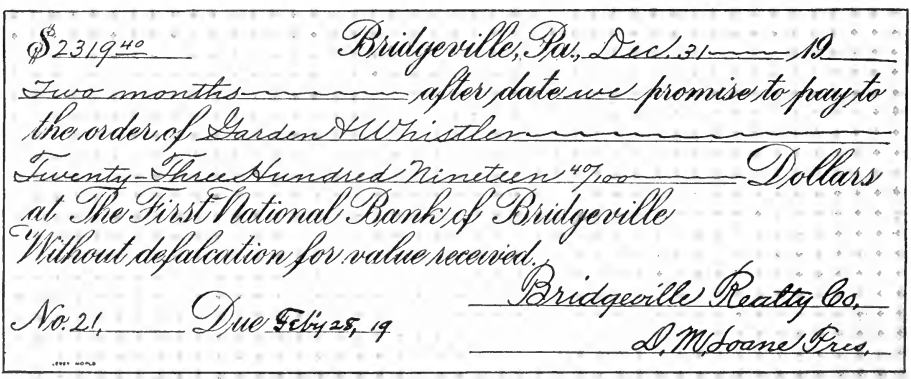
570. Parties. There are two principal (and original) parties to a note, the *maker* and the *payee*. The maker is the party who signs the note—who makes the promise. The payee is the party in whose favor the note is made—the one to whom the money is to be paid.

PROMISSORY NOTE.


$456.25
Buffalo, N.Y. June 10, 19
Thirty days after date I promise to pay
to the order of Henry M. Prentiss
Four Hundred Fifty-six 25/100 Dollars
THE PEOPLES BANK OF BUFFALO
AT THE PEOPLES BANK OF BUFFALO, N.Y.
Value received
Due July 11, 19
John P. Stewart

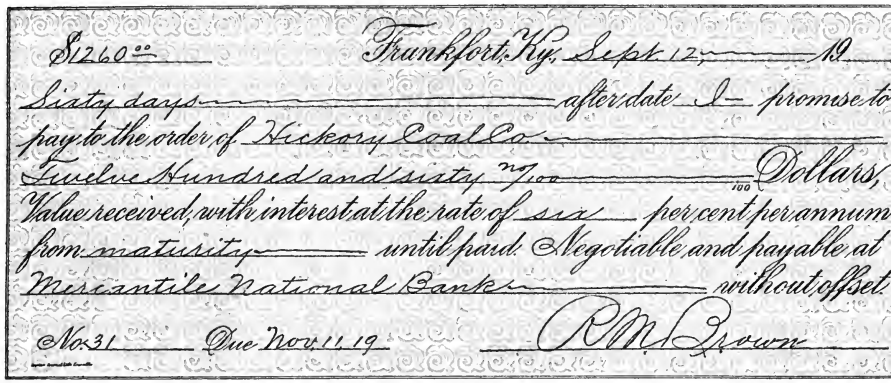
570*a*. In the above note, John P. Stewart is the maker and Henry M. Prentiss is the payee. Observe that the note is made payable at bank, which is presumably the bank of the payee.

PROMISSORY NOTE.


$2319.40
Bridgeville, Pa., Dec. 31 19
Two months after date we promise to pay to
the order of Garden & Whistler
Twenty-Three Hundred Nineteen 40/100 Dollars
at The First National Bank of Bridgeville
Without defalcation for value received.
Bridgeville Realty Co.
No. 21 Due Feby 28, 19
D. M. Doane Pres.

570*b*. In the above note, the maker is the Bridgeville Realty Company, and the payee is Garden & Whistler. Notice that the note, drawn December 31, at two months, matures on February 28, which is the last day of the second month following December. If this note had been made at sixty days instead of two months, the date of maturity would have been March 2.

NOTE WITH INTEREST.



$1260.00 Frankfort, Ky. Sept 12, 19

Sixty days after date I promise to pay to the order of Hickory Coal Co.

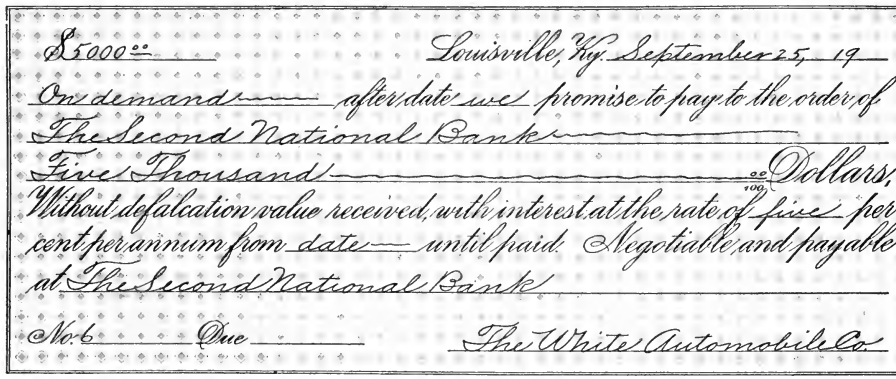
Twelve Hundred and sixty 00/100 Dollars,

Value received, with interest at the rate of six per cent per annum from maturity until paid. Negotiable and payable at Mercantile National Bank without offset

No. 31 Due Nov 11, 19 R M Brown

570*c*. This is a note "with interest from maturity," and shows a form of note sometimes used by merchants in securing settlement of accounts. Notice that the note, which is dated September 12, at sixty days, matures November 11, as October is a thirty-one-day month. A note may be made payable with interest from date of making instead of from date of maturity. A note bearing interest from the date of making is discounted at bank for the amount of the note, that is, the principal plus the interest, which is the maturity value of the note.

DEMAND NOTE.



$5000.00 Louisville, Ky. September 25, 19

On demand after date we promise to pay to the order of

The Second National Bank

Five Thousand 00/100 Dollars,

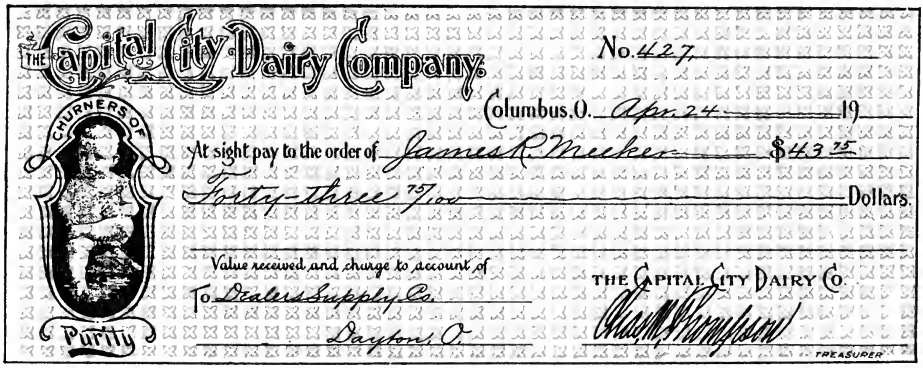
Without defalcation value received, with interest at the rate of five per cent per annum from date until paid. Negotiable and payable at The Second National Bank

No. 6 Due The White Automobile Co.

570*d*. This illustration shows a note payable "on demand," which is a common form of note for borrowing money from bank. A "collateral" note is a similar form of note, with blank space left for a brief description of the collateral. A collateral note may also be made payable a certain number of days or months after date.

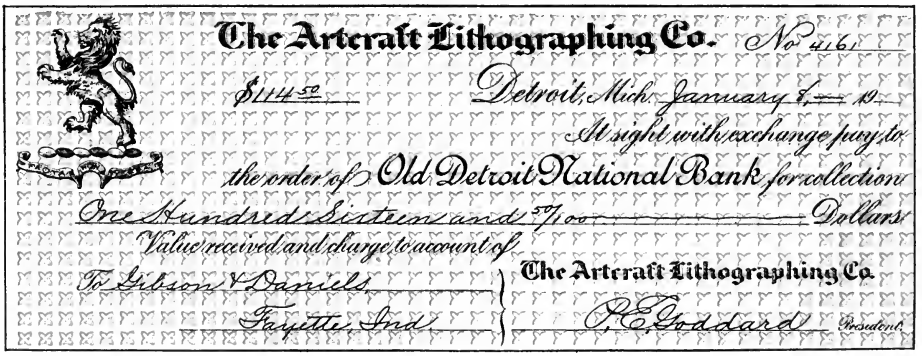
571. A draft is a written request of a first party, or the *drawer*, to a second party, or the drawee, to pay a third party, or the payee, a specified sum of money. The giving of a draft presupposes that the drawer has funds in the hands of the drawee, which will be paid at the time specified in the draft, and also that, if the drawee fails to make such payment to the payee, the drawer will pay. The drawer thus becomes the *first endorser* of the draft.

SIGHT DRAFT.


THE Capital City Dairy Company
No. 427
CHURNERS OF
Purity
Columbus, O. Apr 24 19
At sight pay to the order of James R. Meeker $43 75
Forty-three 75/100 Dollars
Value received and charge to account of
To Dealers Supply Co.
Dayton, O.
THE CAPITAL CITY DAIRY CO.
TREASURER

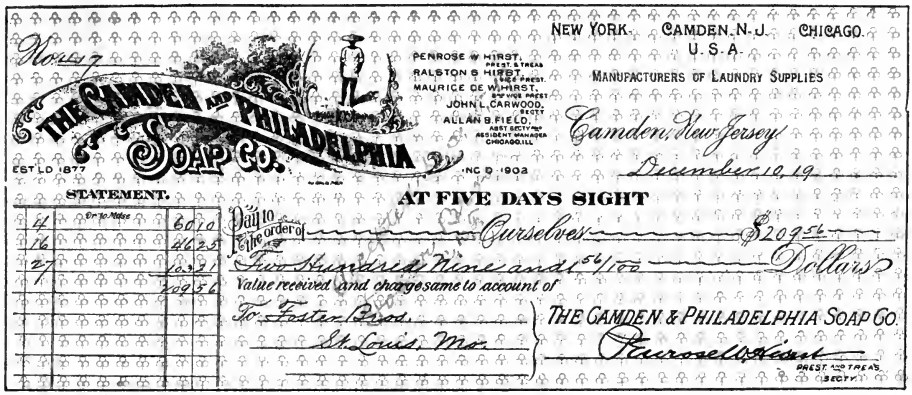
571*a*. In this draft the Capital City Dairy Company is the *drawer*, the Dealers Supply Company is the *drawee*, and James R. Meeker is the *payee*. The draft is sent by the drawer to the payee, who in turn presents it for payment to the drawee. The draft is payable on presentation, being drawn "at sight."

A "COLLECTION" SIGHT DRAFT.


The Arteraft Lithographing Co.
No 4161
$114 50
Detroit, Mich. January 1, 19
At sight with exchange pay to
the order of Old Detroit National Bank for collection
One Hundred Sixteen and 50/100 Dollars
Value received and charge to account of
To Gibson & Daniels
Fayette, Ind
The Arteraft Lithographing Co.
R. E. Goddard President

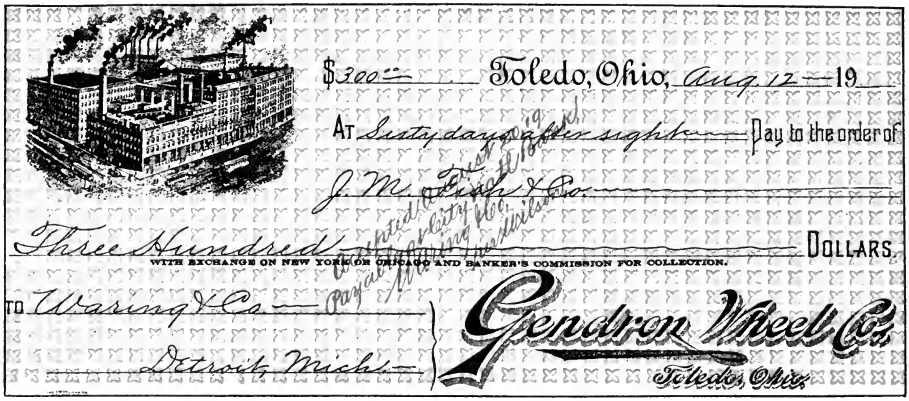
571*b*. Sight drafts are used principally as a means for collecting accounts, in which case they are usually drawn in favor of the bank at which the drawer keeps his account, as shown in the illustration above, or he may draw it in his own favor and endorse it to the bank. When such drafts are deposited for collection, the account of the drawer is not credited until the collection has been made. In the draft illustrated, the Old Detroit National Bank would forward the draft to a correspondent at Fayette, Ind., which would present the draft to the drawee and remit the amount to the Old Detroit National Bank, which in turn would credit the account of the Artcraft Lithographing Company.

A "Collection" Time Draft.



571*c*. The above illustration shows a draft which is similar to the one explained in ¶571*b* except that it is drawn at five days' sight, which means that it is due and payable five days after it has been accepted by the drawees, Foster Brothers; and, therefore, the date of maturity is calculated from the date of the acceptance and not from the date of the draft. In this draft is included a miniature statement of account which is intended to show the items for which the draft is drawn. This is a popular addition to the ordinary draft used for collecting bills. Note that the draft is made payable to the drawer, the drawer and payee thus being the same party. Such drafts are usually remitted directly to the payee, who writes his acceptance across the face of it and returns it to the drawer. It is then known as *an acceptance*. The drawer then deposits it in bank for collection, writing the proper endorsement across the back. When the drawee accepts the draft, he obligates himself to pay it the same as if he had signed a promissory note. In some cases the draft is placed in bank for collection before acceptance, when it is forwarded to a correspondent bank at the point of payment, which presents it for acceptance and holds the acceptance until it is due, when it collects the money and forwards it to the bank from which the draft was received, the same as explained in illustration 571*b*.

An Accepted Draft.


$300.00 Toledo, Ohio, Aug 12 19
At Sixty days after sight Pay to the order of
J. M. First & Bro.
Three Hundred
WITH EXCHANGE ON NEW YORK OR CHICAGO AND BANKER'S COMMISSION FOR COLLECTION.
DOLLARS
TO Waring & Co
Detroit, Mich.
Gendron Wheel Co.
Toledo, Ohio.

571*d*. This draft illustrates an ordinary sixty-day draft, which becomes due and payable sixty days after the date of the acceptance, August 20, which is October 11.

An Accepted Time Draft.

571*e*. This draft differs from the preceding draft in being drawn "after date" instead of "after sight;" consequently, after acceptance, it becomes due and payable sixty days after March 15, or June 14, irrespective of the date on which it was accepted.

572. Drafts are of two kinds as to time of payment, as shown in the preceding illustrations. Those payable "at sight" are known as *sight drafts* and are usually payable on presentation. Those payable "after sight" or "after date" are known as *time drafts*. After a time draft has been accepted, it is known as *an acceptance*.

573. Accepting a draft is agreeing to pay it when it is due by writing the word "Accepted" across the face, followed by the date and the name of the drawee, who thus becomes the "acceptor," and the draft is known thereafter as an "acceptance," as stated in the preceding paragraph.

574. The date of maturity is the date on which the note or draft falls due. When the time is indicated in days, the *exact number* of days is meant, not counting the date of making or of acceptance, but counting the date of maturity. When the time is indicated in months, the *same day of the maturing month* is the date of maturity.

575. A draft drawn "after sight" begins to mature *from the date of the acceptance,* and when drawn "after date" it begins to mature from the date the draft was drawn without regard to the date of acceptance. A note begins to mature from the date it is made.

576. Due on Sunday or a legal holiday. The law in nearly all states is that when the due date falls on Sunday or a legal holiday, the paper falls due on the *next following business day.* In a very few states they are due on the last preceding business day.

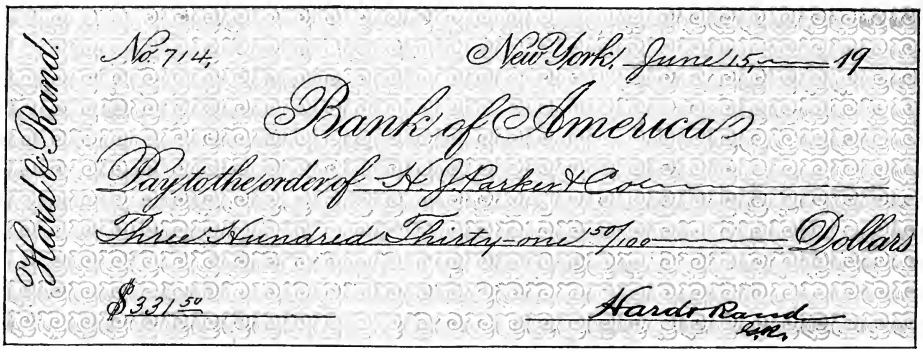
577. Days of grace are three days formerly allowed in addition to the time specified for the payment of commercial paper. They have been abolished in all but a few states, and will doubtless be abolished in all states within a short time.

578. Negotiable notes and drafts are those which can be *transferred* by one party to another. To be negotiable, a commercial paper must contain the words "or order" or "or bearer." When it does not contain these words it is said to be non-negotiable, which means that it cannot be transferred by simple endorsement and delivery. In most states special statutes provide that such papers can be transferred by assignment, though the transferee gets no better title to the paper than the original holder has.

579. Transfer. When a payee transfers a negotiable note or acceptance, he does so by writing his name across the back, and then delivers the paper to the endorsee. This is known as an *endorsement.* When a note is transferred, the payee becomes the *first* endorser; when an acceptance is transferred, he becomes the *second* endorser, unless the draft is drawn by him in his own favor, when he is the *first* endorser.

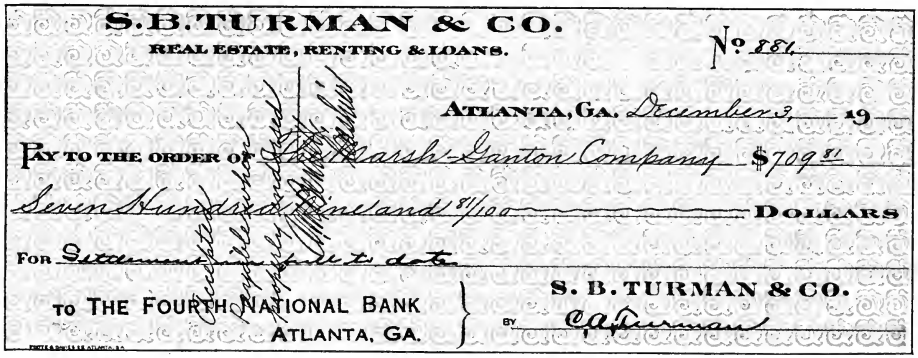
579*a*. When commercial paper is made payable "to bearer," it is not necessary for the holder to endorse it when transferring it to another, but for prudential reasons it is generally requested and usually required. The different forms of endorsement are shown on another page. The endorsements shown apply not only to notes and drafts but to checks and all forms of negotiable paper.

CHECK.


Hard & Rand.
No 714.
New York, June 15 19
Bank of America
Pay to the order of H. J. Parker & Co
Three Hundred Thirty-one 50/100 Dollars
$331 50
Hard & Rand

580. A check is a written order directing a bank or banker to pay money as stated therein. It is presumed that the party writing the check has funds on deposit against which he issues the check. A check is, in reality, no different from a sight draft except in form, the drawee being a bank instead of an individual firm or corporation.

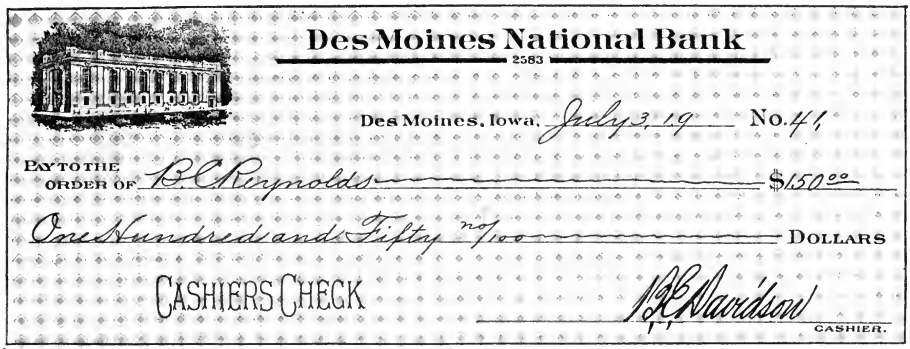
CERTIFIED CHECK.


S. B. TURMAN & CO.
REAL ESTATE, RENTING & LOANS.
No. 881
ATLANTA, GA. December 9 19
PAY TO THE ORDER OF The Marsh-Ganton Company $709 81
Seven Hundred Nine and 81/100 DOLLARS
FOR Statement rendered to date
TO THE FOURTH NATIONAL BANK
ATLANTA, GA.
Certified Dec 9 1907
Payable through Clearing House
S. B. TURMAN & CO.
BY C. A. Turman

581. When a check has been "certified" by a bank as shown in the illustration, the bank becomes responsible for its payment. When a bank certifies a check it is immediately charged to the account of the drawer.

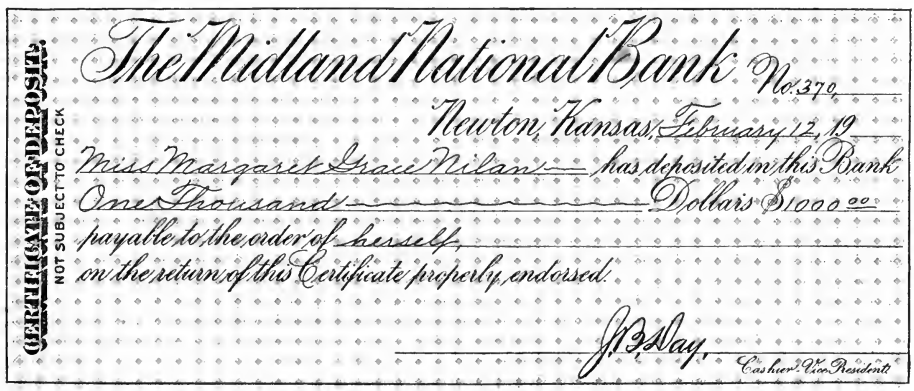
582. A cashier's check is a form of check issued by banks in paying money to those who are not depositors, and is usually signed by the cashier, or it may be signed by the president or any authorized officer.

CASHIER'S CHECK.


Des Moines National Bank
2583
Des Moines, Iowa, July 3, 19 No. 41
PAY TO THE ORDER OF B. C. Reynolds $150.00
One Hundred and Fifty no/100 DOLLARS
CASHIERS CHECK
W. B. Davidson
CASHIER.

583. A certificate of deposit is an instrument issued by banks certifying that the party named therein has deposited funds to the amount stated. Such deposits draw interest when made for a definite period, but, unless otherwise stated, certificates of deposit are payable on presentation.

CERTIFICATE OF DEPOSIT.


CERTIFICATE OF DEPOSIT
NOT SUBJECT TO CHECK
The Midland National Bank No. 370
Newton, Kansas, February 12, 19
Miss Margaret Grace Milan has deposited in this Bank
One Thousand Dollars $1000.00
payable to the order of herself,
on the return of this Certificate properly endorsed.
J. J. Day,
Cashier Vice President

584. A receipt is a written acknowledgment of money received, generally setting forth the purpose for which it was paid.

RECEIPT.

Hinchman, Vezin & Co.

New York, January 10, 19

Received of Hart Mercantile Company

Four Hundred Twenty-eight $\frac{35}{100}$ Dollars

in settlement of invoice of December 18th 19

$428.35

Hinchman, Vezin & Co.

per A. S. Snyder.

585. A bill is a statement setting forth the amount of a debt, usually for goods sold or services rendered, with items, prices and terms stated in detail. A bill, when received from others, is often known as an invoice.

BILL.

All claims for correction must be made within 15 days of date of invoice

New York, March 25 19

Mess Hale & Martin 106 Broad St. Newark N.J.

To Frederick F. Goodman Dr

INCORPORATED

STORAGE CHARGED BY THE MONTH. LESS THAN A MONTH AT TRANSIENT RATES.

AUTOMOBILES

STORAGE, REPAIRS, SUPPLIES, ETC

TELEPHONE 6700 RIVERSIDE

51-55 WEST 93rd STREET

1 White Steamer Model O O #7361	2000				
1 White G.B. Gasoline Car #7412	2500				
1 Courier Gasoline Car Model A30 #1778	1075		5575		
Less 12½%			698	88	
			4876	12	

586. An order is a written request of a first party to a second party, either in favor of a third party or the first party, usually to pay money or deliver goods. It closely resembles a draft, except that the time of payment is not usually indicated, and it is generally less formal in expression.

MONTHLY STATEMENT.

Middletown, Conn. Feb 1, 19__

Mrs John D Wilson & Sons

Portland, Me

To The Rogers & Hubbard Co. Dr.

Jan	1	To Balance	208	50		
	12	To Amount Bill rendered	71	56		
	25		116	45	396	51
		Cr.				
Jan	10	Cash	100			
	15	"	108	50		
	30	"	71	56	280	06
					116	45

587. A statement of account is a statement of an open account showing its present condition. It may show only the amounts of the debit and credit items, or the nature of each item may be specified in detail.

SHIPPING INVOICE OR STATEMENT.

A. L. GARFORD, President
C. E. HADLEY, General Manager

HAYDEN EAMES, Genl Sales Mgr
M B & H H JOHNSON, Counsel

THE GARFORD COMPANY.

ELYRIA, OHIO.

ALL AGREEMENTS MADE SUBJECT TO STRIKES, FIRES AND OTHER CAUSES OF DELAY BEYOND OUR CONTROL

October 3, 19

Messrs. G. M. Hammell & Co.,

Newark, N. J.

Gentlemen:

We are shipping you today, via Lake Shore and Erie Railroads, L. S. and M. S. car 15,416, per bill of lading enclosed, to be sold for our account, at our risk, on terms stated in yours of September 25:

1000 baskets Concord grapes - 8 lbs.

360 " Catawba " - "

200 bbls. Northern Spy apples.

Freight charges prepaid to Dunkirk, N. Y., $7.86.

This fruit was shipped in first-class condition. We trust you will find a ready market, at good prices. Please remit proceeds promptly.

Very truly yours,

C. E. Hadley, Gen'l Mgr.

588. A shipping invoice is an itemized statement of goods or property shipped to be sold on commission for the account of the consignor.

589. An account sales is an itemized statement of sales and charges rendered by a commission merchant or agent to the consignor.

AN ACCOUNT SALES.

TELEPHONE 8972 BELL

G. M. Hammell & Co.

COMMISSION MERCHANTS

AND DEALERS IN FRUITS & PRODUCE,

EGGS & POULTRY.

48 Commerce Street. NEWARK, N. J. October 14, 19

The Garford Company,

Elyria, Ohio.

Gentlemen:

The following is an account of the sales of grapes and apples shipped by you October 3, received October 6, which were sold, at the best market prices obtainable, for your account:

760	baskets Concord grapes,	6,050 lbs.,	at $	.01 3/4	$105.88
240	" " " ,	1,910 "	"	.02	38.20
360	" Catawba " ,	2,890 "	"	.02 1/4	65.02
165	bbls. Northern Spy apples,		"	1.80	297.00
35	" " " " ,		"	1.65	57.75
					563.85

We deduct charges as follows:

Freight, $18.50; drayage, $3.75; commission (6%) $33.83 - Total 56.18

Net proceeds $507.67

You will find our check for the proceeds enclosed herewith.

Trusting that this account of sales will be satisfactory to you, and that we may receive further consignments, we are,

Very truly yours,

G. M. Hammell & Co.

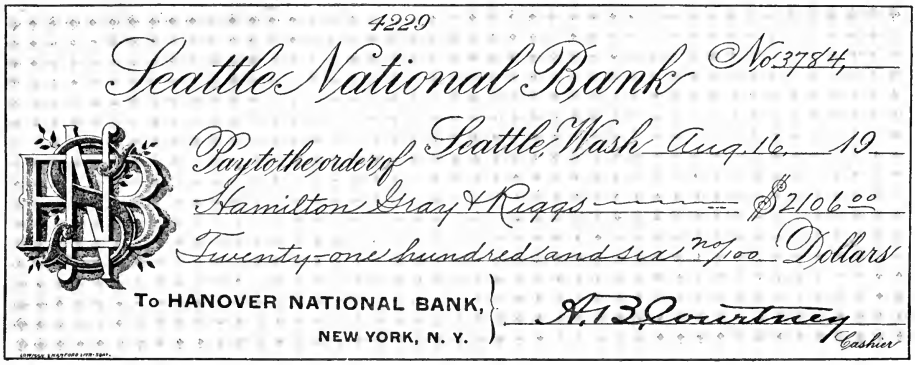
by

590. Bill of Lading. A bill of lading is a receipt for goods delivered to a transportation company for shipment, and usually states certain conditions affecting the reponsibilities of the latter for the care and delivery of the goods.

591. A voucher is a term applied to any paper or document that vouches the truth of an account or confirms a business fact.

592. A bank draft does not differ from an ordinary sight draft except that it is drawn by one bank on another bank, and is made payable to the order of a third party, and is, therefore, a convenient and safe way to make remittances of money, as it is generally collectible, in cash, anywhere, when the payee is identified.

BANK DRAFT.


4229

Seattle National Bank No. 3784

Pay to the order of Seattle, Wash. Aug. 16, 19

Hamilton Gray & Riggs $2106.00

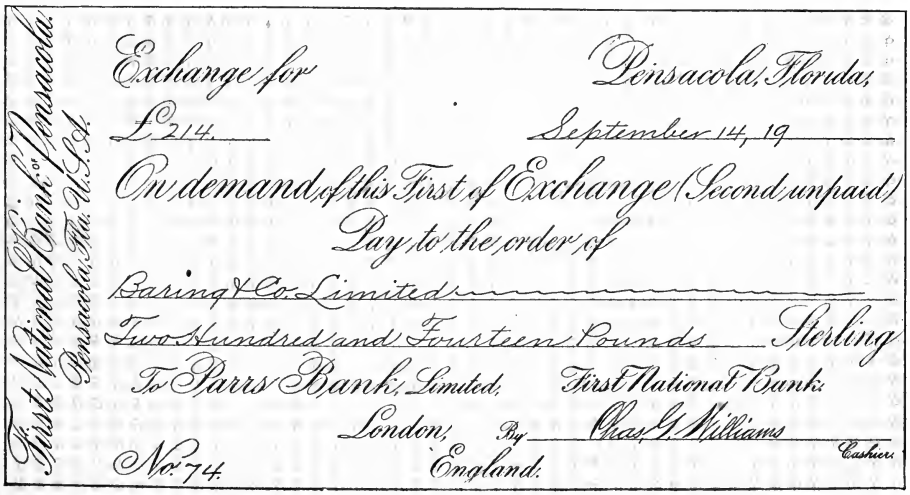
Twenty-one hundred and six no/100 Dollars

To HANOVER NATIONAL BANK, NEW YORK, N. Y.

A. B. Courtney Cashier

593. Bills of exchange are similar to bank drafts, except that they are usually drawn in duplicate for the same amount, the object being to provide against loss of the paper or delay in reaching the payee by mailing them on different days or by

BILL OF EXCHANGE.


First National Bank of Pensacola, Pensacola, Fla. U.S.A.

Exchange for Pensacola, Florida,

£214 September 14, 19

On demand of this First of Exchange (Second unpaid)

Pay to the order of

Baring & Co. Limited

Two Hundred and Fourteen Pounds Sterling

To Parrs Bank, Limited, London, England. First National Bank: By Chas. G. Williams Cashier

No. 74

different routes. Bills of exchange are usually employed in making remittances to foreign countries.

594. Filing of business papers. This is a most important feature of modern office practice. There are many devices and plans for the filing of business papers and letters, the object being to locate them so that they may be easily and readily referred to at any future time. It has become the common practice to file all checks, notes, drafts, etc., with the original bill for which they were issued in payment. For instance, if a bill is paid by note, and later the note is paid by check, both the note and the check should be filed with the bill. This note not only exhibits the entire transaction in case of future reference, but it also keeps the papers in the most convenient form for audit. This is one of the features of the voucher system which has made it so popular.

595. Auditing accounts consists of the accounts of a business being examined and verified with the original business papers or vouchers by an accountant, auditor or other authorized party. The accounts of banks, and of trust, transportation, insurance and similar public companies and corporations are audited at stated intervals, and the practice is rapidly extending to private corporations and firms.

ACCOUNT BOOKS.

596. As previously stated (¶454), journalizing is the *classification* of transactions. This classification is greatly simplified by providing a special book for each kind of transactions, and where there are a great many transactions to be recorded, this plan permits of the work being distributed among a number of bookkeepers, clerks, etc. For these and other reasons, account books vary greatly in number and design, depending largely upon the extent and nature of the business conducted. Books with special columns and other features designed to show certain desired results are found in almost every office, and in this respect wonderful advancement has been made in recent years.

597. It should be remembered that no arrangement of books or system of accounts can be shown which would be applicable for use in every line of business. While the various sets illustrated in this work are accurate representations of standard bookkeeping methods in the various lines of business represented, certain modifications would likely have to be made to exactly meet the requirements of a particular business. Whether or not specially designed books or the use of special columns in any book can be used profitably, depends upon the classification of accounts employed, the amount of detailed information desired, and particularly upon the frequency with which similar transactions occur.

598. To organize the very best system of accounts for a particular business, which will show those results which will be of the greatest value in its management, requires the services of one possessed of a high order of accounting ability, skill and experience.

CASH BOOK.

599. In this book the entries for all cash received and all cash paid out are recorded. It shows receipts and payments of cash. It is used as a posting medium, no cash items, therefore, being entered in any other book.

600. All items of *cash received* are entered on the left or debit side of the cash book, and are posted to the right or credit side of the ledger account named.

601. All items of *cash paid out* are entered on the right or credit side of the cash book, and are posted to the left or debit side of the ledger account named.

602. *The difference* between the two sides of the cash book shows the balance of cash which should be on hand, that is, the cash in safe or drawer plus that on deposit in bank. Cash should be footed and proved daily, and the cash book should be ruled up at least once monthly, or, if desired, it may be ruled up daily or weekly. A simple form of the cash book is shown in illustration 20.

PURCHASES BOOK.

603. This book receives the entries for all purchases of merchandise. There are many forms of this book, their purpose, however, being the same. Each party from whom a purchase is made is credited for the amount in his account in the ledger, and "Purchases" is debited for the total amount of purchases for the month, unless separate purchase accounts are kept for different lines of goods handled, when a special column is kept for each account.

604. "Cash purchases," a term that is applied to bills which are paid immediately, may be disposed of in two ways, either by entering the bill in the usual way in the purchase book and the cash paid in the cash book, checking the one against the other, or by debiting the purchases account directly from the cash book, for which a special column for that purpose may be kept, if desired.

SALES BOOK.

605. This book receives the entries for all sales of merchandise *for which bills are made out*, whether paid for at once or later. This book is also used as a posting medium. Each party to whom a sale is made is debited for the amount of the sale in his account in the ledger, and the total footing for the month is posted to the credit side of the sales account in the ledger, thus preserving the equality

of debits and credits. If separate sales accounts are kept for different lines of goods, special columns may be kept in this book for that purpose. In addition, other special columns, which will be described in the various sets of this work, may be used.

606. Some difficulty is experienced by beginners in distinguishing between "cash sales" and sales that are made on "terms cash" or for "spot cash." *Cash* sales refer to those sales in which goods are delivered and paid for at once, for which no account is kept with the buyer in the books of the concern, the goods being delivered and the cash received as in the case of cash sales in retail stores. For cash sales it is the custom to make out a cash slip or to use a cash register, or both, and at the close of each day's business the total cash received for cash sales must equal the total amount shown by the cash slips or cash register. This amount is then entered directly into the cash book to the credit of sales account, or in a department store to the credit of the several department accounts of the business, if such are kept. Cash sales are, therefore, not entered in the sales book.

607. Sales "terms cash" or for "spot cash," however, are treated differently. In a wholesale or jobbing house, "terms cash" generally means that cash may be paid any time within ten days, and in many lines of business within thirty or even sixty days. "Spot cash" generally means that the goods are paid for as soon as sold and billed to a customer. In either case, the entry is made in the sales book *the same as if the goods were sold on account.* If the cash is received at once, the entries in the cash book and the sales book may be checked one against the other, which debits cash and credits sales, without passing through a personal account. If the sale is made to a regular customer, however, it is the rule to pass the transaction through his account by debiting him in the sales book and crediting him in the cash book.

NOTE AND ACCEPTANCE BOOKS.

608. The *notes receivable book* and *notes payable book* are kept to show a record, in detail, of all the notes and acceptances received and issued. These books are designed to show all the particulars pertaining to each paper in a compact form for ready reference, especially as to its date, maturity, the parties thereto, and its final disposition. These books are used as posting mediums, all entries being posted directly to the ledger, although they may be posted through the journal. When used as posting mediums, the total of the notes and acceptances received and issued for the month or other period are posted to their proper accounts in the ledger, the several contra entries being posted to the different accounts named.

THE JOURNAL.

609. This book is kept to receive only such entries as cannot properly be made in any other book. It may include special columns for different purposes, although many forms of this book, which were once quite popular (for instance, the six-column journal, the special columns of which have been nullified by the cash, purchase, sales and other books) are now almost obsolete. However, the journal still remains an important book, and in many lines of business is susceptible of great utility by the introduction of special columns.

610. The *cash journal* is a combination of the cash book and journal, which is very popular in some lines of business. It is fully illustrated in one of the sets accompanying this work.

OTHER BOOKS.

611. There are many other books in common use in which transactions are recorded, each usually designated by a name indicating the purpose for which it is kept, such as the voucher register when the voucher system is used, the commission sales book or ledger and account sales register used in commission houses, the time book, pay roll book, cost book, and many others used in manufacturing lines, and a number of special books used in banking and financial concerns, which are fully described in the various sets illustrating the various lines of business.

THE LEDGER.

612. As described in ¶ 17, this is the book of accounts. It is the book to which the items and totals of the various books in which transactions are classified and recorded are transferred. It is from this book that the trial balance is taken, and it is from the trial balance that the trading and profit and loss statements, the statement of resources and liabilities, and other statements which show the results of the business for the fiscal period covered are prepared.

613. Ledger accounts may be classified as general accounts, accounts receivable, accounts payable, etc. The general accounts may be kept separately in a general ledger, or these accounts may be again sub-divided into those kept in a general ledger and those kept in a private ledger, the private ledger usually containing those accounts which show the proprietary interests of the owners of the business. Accounts receivable may be kept in a separate ledger known as a sales ledger, and the sales ledger may again be sub-divided into a city ledger and a country ledger, or an Eastern ledger and a Western ledger, or, where there are many accounts, several ledgers may be kept, as "Ledger A to M," "Ledger N to Z," etc. Accounts payable may be kept in a separate purchase ledger. In banks, the accounts with depositors

are kept in a ledger known as the individual or depositor's ledger. A number of ledgers may also be kept for these accounts in divisions of the letters of the alphabet.

CLOSING THE LEDGER.

614. This is a term used to express the closing of the books at the end of each fiscal period, which is usually once a year, although books may be closed every three or six months, or even monthly, which, however, is unusual. "Closing the books" is another term used to indicate the same proceeding. The purpose of closing the ledger, as stated in ¶247 and ¶447, is to *indicate the close of a business period,* and thus to eliminate all open current trading and profit and loss accounts in the ledger preparatory to their receiving the entries of a new business period. Accounts showing resources and liabilities and those showing fixed reserve, surplus, sinking fund or other similar accounts are not closed except in the following cases: (*a*) when an adjustment of the account has been made and it is desired to show the correct balance in one amount, and (*b*) when the space allotted to an account is filled and it is necessary to forward it to another page or to a new ledger. This applies to all excepting the cash account, which is usually balanced, footed and ruled and the balance carried down or forward at least once monthly. When it becomes necessary to forward an account showing a resource or a liability to a new page or a new ledger, only the balance shown by the account should be forwarded and not the footings.

615. Preparatory to closing the ledger, all inventories should be taken and adjusting entries for them and for any other items should be made, after which the final trial balance is taken. The various trading and profit and loss statements and the statement of resources and liabilities are then prepared and proved, after which the entry or entries to close the trading, the profit and loss, and such other accounts as are to be closed, and to distribute the net profit or the net loss to the proper accounts, are made up and entered in the journal. When the items of the closing entry or entries have been posted, and the accounts footed and ruled, the ledger will again be in its primal condition, showing open accounts which should agree with those shown by the statement of resources and liabilities. The ledger is then ready to receive entries for the next succeeding fiscal period.

ERRORS IN TRIAL BALANCES.

616. This subject may be discussed to best advantage under three heads: (1) preventing errors, (2) finding errors, (3) correcting errors. It is better to be expert in avoiding errors than expert in detecting them.

616*a*. *Preventing errors.* One source of errors is in posting to the wrong side of accounts. These errors can be prevented to a large extent by posting the debits first and afterwards the credits from each book. Another plan is to have the pages or books from which debit items are posted paged in even numbers, and the pages or books from which credit items are posted paged in odd numbers. Under this plan, the sales book, and the credit side of the cash book, which contains debit items, would be paged in odd numbers, as 1, 3, 5, 7, etc., while the purchase book, and the debit side of the cash book, which contains credit items, would be paged in even numbers such as 2, 4, 6, 8, etc. Other books containing separate debit and credit items should be paged accordingly. When the posting books have been thus paged "odd and even," as suggested, all page numbers on the debit side of the ledger should show odd numbers, and those on the credit side should show even numbers. In case of an error, a rapid examination through the ledger will quickly show an item that has been posted to the wrong side of an account.

616*b*. In forwarding footings in posting books, or from one account to another in the ledger, care should be observed to place them in the proper columns without transposing the figures. Transposition of figures is a very common source of error in posting and forwarding amounts. Various methods and check systems for finding a transposition of figures have been suggested, but none of them are absolutely certain, and many of them require an amount of work which makes them impracticable. They have been superseded by systematic checking methods which are more practical, one of which is hereafter described.

616*c*. *Finding errors.* Too much importance cannot be attached to a careful checking of each day's postings. The simplest method of checking is described in ¶ 456. One of the *very best* methods of checking is given below.

616*d*. *Reverse checking or proof posting.* This method may be used in connection with any set of books, however large or small. It avoids the use of "check figures," or any of the more or less complicated schemes and devices so frequently met with, and if carried out as indicated will make errors in posting practically impossible. The plan is as follows:—only one book is posted to the ledger at a time. As each item is posted to its ledger account, a slip of paper (say two by six inches in size) is inserted at the account, with the end of the slip protruding slightly at the top of the book. When the posting from each book is completed, beginning with the first slip in the ledger, each unchecked item in the ledger is entered on a sheet of paper ruled in columns and known as a "check sheet." As each item is transferred to the check sheet, it is checked on the ledger account. When all the items posted have been entered on the check sheet, it is footed and the sum of the items on the check sheet must equal the sum of the items posted, as shown by the footing of the column in the posting book. The totals of each succeeding day are added to the footing of the previous day on the check sheet, so that at the end of the month the total footing of the check sheet must equal the total footing shown

in the posting book. Any omissions in posting or transpositions of figures are at once discovered by this method, and if ordinary care is exercised, accounts posted to the wrong side of the ledger will also be discovered. If more than one item is posted to the same account from the same book, a separate slip should be inserted for each item. Separate check sheets should be kept for each posting book. These sheets are generally known as "cash check sheets," "sales check sheets," etc.

616*e*. *The adding machine* may be used very advantageously to prove postings, whether to principal or subsidiary ledgers, in connection with the method of reverse checking and proof posting explained in the preceding paragraph. When the monthly trial balance is "out", the adding machine may be used to prove the postings from any book by finding the sum of all the postings from that book found in the ledger for the month. In like manner the controlling account for any subordinate ledger may be proved.

616*f*. When credits to customers' accounts, which are generally made to cover a specified bill or bills, are posted, if canceling items on each side of the account are carefully compared and indicated by placing a small cross-mark or letter to the left of the amounts, it will generally discover any errors which have been made in entering the wrong amount, while it leaves the account in the best shape to quickly ascertain the correctness of subsequent payments on the account.

616*g*. *Correcting errors.* When an error is found, it should never be corrected by an erasure. If an item has been posted to the wrong side of an account, or if the wrong amount has been posted, a red line should be ruled through the amount and the proper entry made. When necessary, adjusting entries in the journal may be made. Such entries, however, should contain a full and explicit statement of the error and of the correction made, so that at any time it would be perfectly understood.

617. A Corporation was defined by Chief Justice Marshall as "an artificial being, invisible, intangible, and existing only in contemplation of law." It is sometimes termed an "artificial person."

617*a*. *Corporations are necessary* to provide a convenient means of combining the funds which a number of individuals may have for investment, in order to supply the capital required to conduct and carry on large commercial and industrial enterprises without requiring those who contribute this capital, whether in large or in small amounts, to assume the responsibilities and liabilities of the ordinary partner; consequently, laws have been enacted by the legislatures of the different states creating for corporations a separate legal existence, and extending to stockholders certain privileges and exemptions from liability, and other advantages which cannot be secured in the ordinary partnership relation. Corporations, as a rule, may be formed for any legitimate purpose.

617*b*. *Corporations are created* in two ways, by *charter* and by *general statute*. When created by charter, a special act must be passed for each corporation, which is known as its *charter*. This charter defines its powers and privileges. When created by general statute, all that is necessary is to comply with the provisions of the statute, which defines its powers and privileges. Nearly all corporations are now created by general statute, and very few by special charter.

617*c*. *The method of procedure* in forming a corporation by general statute is very simple. The required number of individuals (not less than two and usually not less than five) join in a written instrument known as "Articles of Incorporation," which, when properly acknowledged before some competent officer, is submitted to the judge of a court for his examination as to whether or not it conforms with the law creating it, and when properly approved and certified by him it becomes a *certificate of incorporation*, the act under which the corporation is formed being its charter. After this certificate is properly recorded the corporation is formed, and when by-laws are adopted and the board of directors and officers are elected the corporation is ready to proceed in conducting the business for which it was created.

NOTE—The legal part of the formation of a corporation should invariably be entrusted to an attorney.

618. Terms and definitions. There are certain terms and definitions used in connection with corporations with which you should be familiar. Some of them are here described.

619. The capital stock is the amount of stock authorized by the charter or certificate of incorporation, at its par value. *The paid-in capital* is the amount paid on the subscribed shares of stock by the stockholders.

620. Treasury stock is stock of a corporation which has been previously issued to stockholders, and is later purchased from the funds of the corporation or is secured by donation or gift. Unissued shares of the authorized capital stock must not be considered as treasury stock. Treasury stock does not participate in dividends. "Treasury stock is the stock of a company issued as fully paid, which subsequently comes back to the company: (*a*) as settlement of an account due the company; (*b*) as a purchase by the company; or (*c*) as stock donated for working capital."

621. The stockholders of a corporation are the individuals who own the property of the corporation, each stockholder's interest being measured by the number and value of the shares he holds.

621*a*. A stock certificate is a document issued by the corporation to each stockholder, certifying that he is the owner of a certain specified number of shares of the capital stock of a specified par value.

622. The board of directors is elected by the stockholders and represents them. It is vested with the management and direction of all the affairs of the corporation through its officers, who are generally elected from among its own number. These officers are usually a president, vice-president, secretary, and treasurer, whose duties are defined in the by-laws.

623. The president is the chief executive officer, who presides at the meetings of the board and ordinarily exercises the authority of the board when it is not in session.

624. The secretary keeps the official records of the corporation. He is custodian of and is responsible for the charter and seal of the corporation, and for the minute book and the various other books containing the records relating to the stockholders of the corporation. The most important of these books are:

(*a*) *The minute book*, in which is recorded the proceedings of all the meetings of the stockholders and of the board of directors. This record should be most complete, as the officers must look to it for the necessary authority to conduct the affairs of their respective offices, and in case of litigation it is taken as *prima facie* evidence for the acts of the board of directors and officers. It should contain the by-laws of the corporation, and the minutes of each meeting should be signed by the secretary and also by the president.

(*b*) *The stock certificate book* is a book of printed certificates, with stubs, which are filled out and issued to the stockholders.

(*c*) *The transfer book*, or journal, receives entries for all transfers of stock from one stockholder to another and from it the proper entries are made in the different accounts in the stock ledger. Entries for *the original certificates* issued may be entered in this book also, and posted from it to the stock ledger. When this is done, the amount of the original stock issued should be charged to "Capital Stock Issued" account in the stock ledger, which would then show a debit balance equal to the credit balance shown by the capital stock account in the general ledger, as well as the sum of the credits to the various stockholders' accounts in the stock ledger, thus making the stock ledger self-balancing.

(*d*) *The stock ledger* contains the accounts with the different stockholders, and shows the number and the par value of the shares of stock owned by each. It is a subordinate ledger, of which the capital stock account in the general ledger is the controlling account. It receives its entries from the stock certificate book and from the transfer book. From the stock book, each stockholder is credited for the number of shares and the par value of the stock issued to him. From the transfer book, he is debited for the number of shares and the par value of stock transferred by him to others. The balance shown by each account is the par value of the stock owned by the stockholder.

(*e*) *The dividend book* is kept to show the dividends declared and paid to each stockholder. A dividend is a certain percentage declared on the capital stock to be paid from the surplus earnings of the company.

625. The treasurer is the financial officer of the corporation. He is usually the custodian of and is responsible for all the funds of the corporation. The ordinary books of account in which is recorded the general business of the company are kept in his office. It should be remembered that the books of the secretary and those of the treasurer are distinct and separate, although the duties of one, either in whole or in part, may be and frequently are performed by the other, to suit the requirements of a particular business or as required by the board of directors or by the by-laws.

SOME DIFFERENCES BETWEEN PARTNERSHIPS AND CORPORATIONS.

626. Formation. *A partnership* is an association of two or more persons for the purpose of conducting a business and sharing in the profits and losses accruing, with all the powers and privileges under the law that each partner enjoys as an individual. *A corporation* is an association of individuals authorized by law to act as a single person, with powers and privileges restricted to those definitely set forth in its special charter or in the general corporation statute (act) under which it is formed.

627. How formed. A partnership is formed by an agreement (either written or verbal) between two or more persons to contribute capital, ability or service, or all of them, for a certain purpose, and the associated partners are known as a *firm*. A corporation is formed by the association of two or more per-

sons under a special charter or under a certificate of incorporation issued by some officer of the state, in accordance with the general or special law under which it is created, and is usually designated as a *company*.

628. Liability. In a partnership each partner is liable *for all the debts of the firm*. In a corporation each stockholder is liable only for such an amount as is defined by law, which is usually the amount of his stock, but always in proportion to his share in the capital stock of the corporation.

629. Continuation. A partnership continues until the expiration of the time agreed upon for dissolution or until the death or legal disability of one of the partners. A corporation continues until the expiration of its charter, which may be perpetual. The death or disability of a stockholder does not affect a corporation.

630. Powers. A partnership has no restrictions that the individuals composing it do not have, and it may engage in any line of business so long as it is legal. A corporation is restricted to the performance of only such acts as are necessary to conduct the particular business or accomplish the particular purpose for which it was created.

631. By whom conducted. The affairs of a partnership are conducted by the members of the firm, or such of them or their agents as are so authorized by the agreement between the partners. The affairs of a corporation are transacted only through the officers elected by the stockholders, or their legal representatives, as authorized and defined by the charter and by-laws, who act as agents of the corporation.

CORPORATION ACCOUNTS.

632. The accounts of a corporation are in no way different from those of a firm or an individual proprietor in so far as they relate to the routine transactions of the business conducted, but there are a number of accounts necessitated by the requirements of corporate ownership which are found only in connection with corporation accounting and are not found elsewhere. These accounts relate to the investments of the stockholders and the distribution of profits.

633. Capital stock account. This account, in a way, corresponds with the capital account of a proprietor or partner, since it is an ownership account (read ¶55, 58*b*), and shows the par value of the stock owned by the stockholders; but it is not affected by the gains or losses of the business, which are shown in undivided profits, surplus, and other similar accounts, nor by the purchase and sale of the stock between the stockholders.

Paragraph 663—Continued.

a. It is *credited* for the par value of the stock issued, up to the amount of the authorized stock.

b. It is *debited*, when the capital stock is reduced, for the amount of shares retired and canceled, at their par value.

c. *The balance* shows the amount of stock of the corporation, at its par value, in the hands of its stockholders, and it should equal the sum of the balances shown by the accounts with the different stockholders in the stock ledger. If treasury stock is held, its par value must be added to the sum of the balances in the stock ledger to equal the balance of the capital stock account. Capital stock represents a *secondary liability* of the corporation.

NOTE—It should be credited only for the actual stock issued, and not for the total authorized capital stock unless all of it has been issued.

634. Treasury stock account. This account shows the amount of the capital stock of the corporation previously issued to stockholders, which has been secured from them by purchase, gift or donation.

a. It is *debited* for the *cost* of all treasury stock purchased by the corporation or for the *market value* of stock received by gift or donation.

b. It is *credited* when treasury stock is disposed of, for the *cost* of the stock if purchased or for the *market value* of the stock if received by gift or donation. If sold for more or less than the price charged in the account, surplus account should be debited or credited for the difference between that price and the selling price. If the stock is retired and canceled, credit the account for the amount for which it was debited when the stock was received, and debit or credit surplus account with the difference between that amount and the par value of the stock retired, debiting capital stock account for the par value of the stock retired and canceled.

c. *The balance* shows either the cost or the market value of the treasury stock on hand, which is a resource.

NOTE—Treasury stock does not participate in dividends declared, and in many states the purchase of its own stock by corporations, as treasury stock or otherwise, is forbidden.

635. Subscription Account. This account is opened to show the par value of stock which has been subscribed but not issued. It is credited at par value for the amount of stock subscribed and not issued at that time; it is debited for such stock when finally issued. The balance, if any, shows the par value of stock subscribed but not issued.

636. Reserve, surplus and undivided profits accounts. (Read ¶557 to 557*d* inclusive, page 167.)

Accounts Debited and Credited in Connection with Transactions Relating to the Stockholders of a Corporation.

637. In disposing of the transactions relating to stockholders in the books of a corporation, the names of the accounts to be debited and credited are given, following each proposition stated:

a. Where stock is subscribed and immediately paid for:

Cash, Dr. — For par value of the stock sold.
Capital Stock, Cr.

b. Where stock is subscribed and not all paid for at one time:

Subscriber, Dr. — For total amount of stock subscribed, at par value.
Subscription %, Cr.

c. When part of the subscription price is paid when stock is subscribed, or when part is paid later:

Cash, Dr. — For the amount paid in cash or otherwise.
To Subscriber, Cr.

d. When subscribed stock has been paid for in full and the stock issued:

Subscription %, Dr. — For the amount of stock issued, at par value.
Capital Stock %, Cr.

e. When stock is subscribed and payment made by cash, notes and property, *i.e.*, if A, B, and C each subscribed for twenty shares of D Company stock, par value $2000—A pays cash, B pays half cash and the balance by note at thirty days, and C deeds to the company land appraised at $2000:

Cash, Dr.	$2000		For amount of stock issued and paid for, at par value, by A.
Capital Stock, Cr.		$2000	
Cash, Dr.	1000		For amount of stock issued and paid for, at par value, by B—one-half cash and one-half note.
Notes Rec., Dr.	1000		
Capital Stock, Cr.		2000	
Land, or Real Estate, or Cost of Property, Dr.	2000		For amount of stock issued and paid for, at par value, by C, in land.
Capital Stock, Cr.		2000	

In like manner, if the stock was paid for by a patent right, machinery, services or other value, a corresponding account, under an appropriate title, that would clearly set forth the nature of the transaction should be debited, such as "Patent Rights" %, "Machinery" %, "Cost of Property" %, etc.

f. E, F, and G are partners. They decide to incorporate their business, each taking stock for his interest in the old concern. If the business is to be recorded in the old books, the entry to adjust is:

E, Dr.
F, Dr. — Each for the amount of his net capital in the firm, for which he has received stock in the new company at par.
G, Dr.
Capital Stock, Cr.

If they desire to open a new set of books, the accounts shown by the statement of resources and liabilities would be debited and credited for the amounts shown therein, in connection with the entry shown above.

If stock was sold to additional stockholders, the entry would in every way be similar to those given in previous examples under like conditions.

g. H and I are partners, each with a net capital of $25,000 shown in their capital accounts. They decide to incorporate with a capital stock of $100,000, of which they are to receive $75,000 par value in payment of their interest in the former business, represented by their capital stock, the $25,000 being for good-will. The remaining $25,000 was disposed of to outsiders, at par value. The entry to adjust is:

H, Cap. %, Dr.	$25,000		To close capital %
I, Cap. %, Dr.	25,000		To close capital %
Good-will, Dr.	25,000		To open
Cash, Dr.	25,000		To transfer to new books
Capital Stock, Cr.		$100,000	

"Cost of Property" is a term that is used to designate the difference between the current assets and liabilities of a business or property purchased and the purchase price. Oftentimes, when it is desired to state the assets purchased, at their cost, on the books of the company, it is necessary to set up an account called "Reserve for Capital Investment." This reserve is sometimes referred to as "Capital Reserve."

h. Where both common and preferred stock are issued to stockholders, their sum equals the capital stock of the company, although separate accounts are opened for each; for instance, in example *g*, if the capital stock of $100,000 was divided into $50,000 preferred stock, $50,000 of common stock, instead of capital stock being credited, preferred stock would be credited $50,000, and common stock $50,000.

i. When stock is sold at a discount, *i.e.*, if J and K purchase ten shares of stock, par value $100, at $75 per share, if the shares are paid for in cash the entry is:

Cash, Dr.	$1500	
Discount on Stock Sold, Dr.	500	
Capital Stock, Cr.		$2000

j. In the above transaction, if one-half is to be paid in cash, the entry is:

J, Dr.	$750	
K, Dr.	750	
Discount on Stock Sold, Dr.	500	
Subscription %, Cr.		$2000

As the stock is paid for, "Cash" is debited and J and K credited. When each has paid $750 for the stock and it is issued, the entry to adjust is:

Subscription %, Dr.	$2000		For the par value of the stock issued.
Capital Stock, Cr.		$2000	

NOTE—The preceding examples illustrate the simpler entries required in opening the stockholders' accounts of a corporation. In these days of holding companies, subsidiary companies, and the many other combinations in corporate ownership, there are many conditions continually arising which require special treatment at the hands of the accountant. This, therefore, is a subject which properly belongs to the most advanced part of higher accounting work and, consequently, is omitted in this text.

MANUFACTURING ACCOUNTS.

638. Commercial and industrial pursuits may be divided into two classes: those of traders or distributors, who are known as merchants, and those of makers or producers, who are known as manufacturers.

639. The merchant *buys* and sells; the manufacturer *makes* and sells, *i.e.*, the merchant buys and sells the finished product, while the manufacturer buys the materials and hires the labor to turn these materials into the finished product which he sells to the merchant. Sometimes the manufacturer acts as his own merchant or distributor by selling his product directly to the user or the consumer, just as occasionally the merchant may manufacture some part of that which he sells.

640. Just as the principal profit of a mercantile or trading business is derived from the *purchase* and sale of commodities and is ascertained from that group of accounts known as trading accounts, so, in like manner, the principal profit of a manufacturing or industrial business is derived from the *manufacture* and sale of commodities, the cost of manufacture being ascertained from that group of accounts known as manufacturing accounts. *The cost of finished goods sold* in a manufacturing business corresponds with the "cost of merchandise sold" in a trading business, the only difference being that in one case the concern makes the goods and in the other it buys them already made. Similarly, the *gross trading profit* shown by the trading accounts of a merchant corresponds with the *gross profit from sales* shown by the accounts of a manufacturing concern.

641. While there are marked similarities between trading and manufacturing accounts, as indicated in the preceding paragraph, they differ in some important respects owing to the great difference in the *elements of cost* entering into the manufacture of goods and the corresponding difference in the *units of information* desired. While the accounts of a small factory may be very simple, in large establishments, where every detail of cost and expense must be shown, elaborate systems must be installed which exemplify the highest expressions of scientific accountancy, and for that reason manufacturing accounts, cost systems, etc., are of special interest.

ELEMENTS OF COST.

642. There are three principal elements of cost in manufacturing, namely: the cost of materials, the cost of labor, and the cost of manufacturing expenses. The items showing these costs are entered into corresponding accounts known as material accounts, labor accounts, and factory expense accounts. The items

entering into each of these accounts may be further classified in separate accounts to any extent desired, in a manner similar to the classification of items in the principal and subsidiary accounts of a trading business. (Read ¶134 to 139)

643. Materials. In a manufacturing sense, material is that of which anything is made. *Raw material* is material in its natural state, or nearly so, such as coal, cotton or wool. Many materials pass through several stages of manufacture before they reach their final form in the finished product; for instance, iron ore is converted into metal by one process, into steel by another, and into its final form by a third and, not infrequently, by a fourth or fifth operation. Consequently, the finished product of one concern or factory or department may become the material of another; for instance, the finished product of the pig iron manufacturer becomes the material of the steel manufacturer, and his finished product, in turn, becomes the material of the engine builder or the tool maker, etc.

644. Labor. This is a most important element entering into the cost of manufacture. It represents the cost of converting the material into the finished product, whether the labor is expended directly upon the material, in the operation of machines, or in other ways connected with the processes of manufacture.

645. Factory expenses, or "shop," or "manufacturing," expenses, as they are variously designated, include the cost of superintendence, incidental labor, supplies, rent, fuel and light, power, taxes on plant, insurance on plant, maintenance, repairs, renewals, depreciation, and such other items as enter into the cost of production. These expenses are, in a general way, similar to the general expenses of a trading business, but they include only those that relate to the particular shop or factory covered in the manufacturing accounts and not to the general expenses of the business, unless they are all included in factory expense, which would be permissible only in rare instances and under very unusual circumstances. (Read ¶310, 314, etc.)

646. To the manufacturer, a thorough understanding of the different elements of cost entering into the manufacture of the goods he makes or produces is of the utmost importance, and since the accounts of a manufacturing concern are, in a large part, a record of these various costs, it is also important that the student of accounts should understand them and their relations to the various manufacturing processes before he proceeds to a detailed study of these processes and of the various manufacturing accounts and records. This leads us to a consideration of cost accounting.

COST ACCOUNTING.

647. Cost accounting refers to that department of accountancy which has for its purpose the ascertaining and recording of the *actual cost of making things, i.e.*, the actual manufacturing cost of a given article or product. It is sometimes called "Costing," and when installed in connection with a particular concern it is generally referred to as a "cost system."

648. Cost accounting is perhaps the least understood of the many subjects relating to accountancy. It is also considered to be one of the most difficult subjects an accountant has to deal with, not because its general underlying principles and the objects to be obtained are so hard to understand, for they are quite simple, but rather because of the trouble experienced in applying these principles to meet the infinite variety of conditions found in connection with different manufacturing processes and establishments. A high order of professional experience and skill is required to work out the details of a satisfactory cost system for a concern of any considerable size, where the manufacturing processes are at all complicated. Cost accounting is, therefore, given a somewhat fuller explanation in this work than would otherwise be necessary, although the discussion is directed to the records and bookkeeping features of the subject rather than to those that relate to shop organization, shop management, labor efficiency, cost installation, etc., which are subjects outside the main purpose of this text, although they are given some incidental attention.

649. It should be understood that cost accounting is not a system of bookkeeping so much as a system of cost records and of methods to ascertain the actual cost of the material, labor, and expenses entering into the finished manufactured product. Cost books and records are separate and distinct from the regular, or commercial, account books of the concern, although the closer they are interwoven and articulated with the various manufacturing accounts of the principal books the better the results flowing from the cost system installed are likely to be. It is, in fact, a study of "cost of production" as well as of cost accounts.

650. Cost-keeping, or cost finding, is frequently considered a specialty in factory management. While a cost-keeper should know accountancy, he may not rank high outside of his specialty. The ability to *ascertain*, *analyze*, and *compare* the facts and conditions of a particular factory or concern is the first requisite. The second is the ability to work out a practical cost system that will suit the facts and conditions as they exist, and give the "units of information" required for efficient management.

651. Modern commercial and industrial methods have made cost accounting a necessity. The margin of profit between cost and selling price of standard commodities has been narrowing steadily as our natural resources have been developed and our trade and manufacturing conditions have become more clearly defined and settled. *The consumer*—the man who buys—is in the market to purchase as cheaply as possible; in fact, all other things being equal, he will invariably buy where he can get "the same goods for less money" or "more goods for the same money." *The merchant*, or trader—the man who sells to the consumer and buys from the manufacturer or producer—transmits this pressure of competition for the lowest possible price back from the man who buys *to the man who makes the goods.*

652. The manufacturer—the man who makes things—must find his profit between the price for which he can sell his products and their "cost to make." He cannot fix his prices higher than the prices of other manufacturers for the same article. He must meet competition. If he would make a profit he must manufacture as cheaply as his competitors, and if he can reduce his "cost to make" below the cost to make of his competitors, he can increase his profit to that extent, and still meet competition.

653. Here we are brought face to face with the necessity of cost accounting, *i.e.*, a system of records and accounts that will show the actual cost of producing any given article or number of articles through every process of manufacture, covering the entire period from the time materials are put in process and the labor is employed which will transform them into manufactured products, until the time the finished article is ready for sale and delivery, and, indeed, until the time when it is sold and delivered to the buyer.

654. What constitutes cost. The cost of an article, as already indicated, may be divided into three parts, namely: cost of material and labor, which are known as "direct charges," and cost of factory expenses, which are known as "indirect charges."

(1) *Cost of material* includes cost of:
- (*a*) The raw article.
- (*b*) Completed parts purchased.
- (*c*) Partially completed parts purchased.

(2) *Cost of labor* includes the cost of *productive* labor directly employed in the manufacturing processes, but does not include incidental labor about the factory or shop not employed directly in the manufacturing processes.

(3) *Cost of factory expenses* ("burden") includes:
- (1) Rent and taxes of factory.
- (2) Depreciation and maintenance of plant, machinery and tools.

(3) Motive power, lighting and heating.
(4) Superintendence.
(5) Unproductive labor, including wages of timekeepers, storekeepers, and those employed for other purposes, such, as cleaning factory, distributing and collecting tools, etc.
(6) Interest on capital invested in materials, supplies, plant, machinery and tools.

654*a*. In addition to the cost of material, the cost of labor, and the cost of factory expenses, stated above, it is sometimes considered that some part of the administrative or "overhead" expenses should be included in the "cost to make."

(1) *Administrative expenses* include:
(1) Salaries of managers, clerks and directors.
(2) Rent, taxes, etc., of show-rooms, and office and general office expenses.
(3) Discounts, allowances, and bad debts.
(4) Interest on capital other than that included under "factory expenses."

(2) *Factory expenses*, or "burden," are always included in the "cost to make," *i.e.*, the production cost of the article. Administrative expenses, on the other hand, are never included in the cost of production unless they contain items which are clearly manufacturing expenses. However, both administrative and selling expenses, with the profit, must be included in finding the *selling price* of the article.

655. A thorough understanding of the different elements of cost entering into the total cost of manufacturing and marketing a given article or line of goods is fundamental in the study and practice of cost accounting. The elements of cost are cumulative in their finding, beginning with the *first, or prime cost*, to which other elements are added until, finally, the selling price of the finished product is determined. *The primary elements of cost* are invariably *material* and *labor*, although the proportions of each entering into different products may vary greatly.

656. Finding costs. The costs represented in material and labor are not hard to determine because they are represented by the actual cost of the materials used and the cost of direct labor as shown on the time cards and pay-roll. The costs of *factory expenses*, or "burden," and such administration expenses or other "overhead" charges as may be considered manufacturing expenses, are somewhat more difficult to determine and, particularly, to properly distribute over the various articles manufactured.

657. Factory expenses consist of all incidental expenses for *indirect labor, supplies and material*, and other items of expense necessary in operating the factory which are chargeable directly to the cost of manufacture. (¶645) These expenses are known as "burden," doubtless for the reason that they must be **borne and provided for** as a part of the factory cost of the articles produced.

658. Overhead expenses are those which are incurred in the administrative department of the concern but which have, in fact, increased the cost of production in the factory, works or plant, either in their management or in technical or clerical service rendered, although instead of being charged directly to factory expense, which is always preferable, are charged in the general or administrative expense accounts of the concern. These are known as "overhead" expenses, doubtless because they represent a manufacturing cost *over and above* those included under the head of factory expense, or burden.

659. It is sometimes difficult to distinguish between what should properly be classed as administrative expenses and those which should properly be considered as manufacturing expenses. An illustration is where part of the services of officers or office employes are given to the manufacturing department and part to the selling or financial departments. Another illustration relates to the proper account to be charged for drawings and patterns.

660. Just what overhead expenses should be included in "factory cost," or "works cost," or "cost of production," as it is variously designated, is a question about which there are differences of opinion. Some hold that all expenses outside of those incurred in effecting sales and in the management of the financial affairs of the concern are necessarily incurred in connection with the manufacturing processes and that they should, therefore, be included in the manufacturing costs in ascertaining the "factory," or "works" cost, or the "cost of production." This view is opposed by the argument that it might very easily be carried to the extreme of including a large part of the administrative or other general expenses in factory expense, which would, in fact, capitalize them by including them in the cost of the goods manufactured, as shown in the finished goods account, and would thus show them as assets in the final statements of the business instead of expenses chargeable against income.

661. Others hold that manufacturing costs should include only those that are incurred in the factory or works proper, and that those incurred in connection with the administration or financial departments of the business, even when including the cost of technical or clerical service rendered to the factory, should in no way be considered as factory expenses and, therefore, should not be included among the elements of cost of production chargeable to orders, jobs or contracts. The point at which the line is drawn between factory and other expenses by those who hold this view is illustrated in a concern having its plant in the country and its commercial office in the city, where only the expenses of the former would be included in factory cost, the expenses of the latter being classed as expenses of conducting the business that, in a bookkeeping sense, should be charged against *income.*

662. There is general agreement, however, that the best practice is to charge all expenses that are classed as factory expenses directly to that account at the time the entry is made, which will avoid any later question as to their proper disposition and will eliminate all questionable items from the administrative or general expense accounts, so that these accounts will then clearly represent balances which should be charged against income and should appear only in the trading and profit and loss statement.

663. A careful consideration of these views would seem to indicate that the line between factory costs and administrative and other costs should be drawn at that point which would include as manufacturing expenses only those items that are clearly a direct element of cost in the production of the manufactured article, no matter in what account they may be found. In any event, what should be considered manufacturing costs and what should constitute administrative and other expenses, and the place at which the former should end and the latter begin, must be decided separately for each establishment in which a cost system is installed, either by the owners or by the accountant. (¶752)

664. The cost formula given below clearly shows the various elements of cost entering into the finished product, from the prime cost to selling price. It agrees substantially with the cost formulas prepared by a number of the leading cost specialists, which are generally accepted as being as nearly accurate as they can be made. The elements of cost may be thoroughly understood from a study of this formula and the graphic illustrations showing cost elements which follow, particularly if the accompanying explanations are carefully considered.

COST FORMULA.

(1) Cost of Material + Direct Labor = First or Prime Cost.
(2) Prime Cost + Factory Expense, or "burden," = Factory Cost, or Cost of Production.
(3) Factory Cost + General and Administration Expenses, or "Overhead," = Total Cost.
(4) Total Cost + Selling Expense and Profit = Selling Price.

665. While "prime cost," "factory cost," and "total cost" are terms commonly used and accepted, there are other terms used to express the same costs which are preferred by some writers. There is general agreement as to what should be included as first or prime cost, but there is some difference of opinion as to what should be included under "factory cost" and "total cost," and as to what proportion, if any, of administrative and general expenses should be included as factory costs, as has already been explained in ¶660, 661.

666. EXPLANATION SHOWING THE RELATION BETWEEN THE ELEMENTS OF COST IN THE FORMULA AND THE MANUFACTURING ACCOUNTS IN THE GENERAL LEDGER.

a. The first, or prime cost is made up of the cost of material and direct labor, and corresponds exactly with the items charged to materials in process and productive labor accounts. (¶711*a*, 716*a*) These items are shown on the shop cards or in the job ledger at the time when the order, job or contract is completed. (¶750, 741*a*)

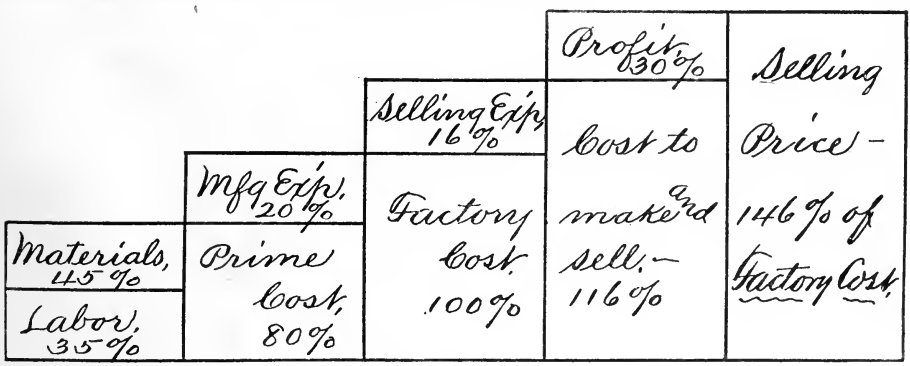
b. Factory cost represents the prime cost, plus manufacturing expense, or "burden." (¶719) The items of factory expense are indicated in ¶645, 734*a*, *b*. The items referred to are those of the factory or works only and not those of the office or general establishment. These factory costs, when distributed, agree exactly with the items credited to the *contra* manufacturing expense account. (¶722*c*)

c. Total cost equals factory cost, plus such general, administrative or other "overhead" expenses, etc., as may be charged to the various orders, jobs or contracts. The items included in the "total cost," or "total cost to make," correspond exactly with those charged to finished goods account. (¶741*a*)

d. The selling price equals the total cost, plus such percentages or other proportions of that cost as are added for selling expenses and for the profit to be made on the goods sold. Selling expenses are not and should never be considered as manufacturing expenses, and should never be included in the production cost of goods manufactured. "Selling price" exactly corresponds to the amount credited to sales count. (¶745)

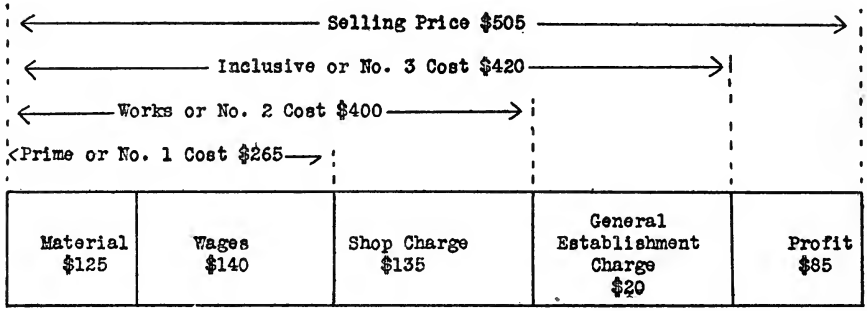
e. The selling expense account of a manufacturing business corresponds exactly with the same account for a trading business. (¶264 to 277) It is a profit and loss account and, like other similar accounts, must be deducted from the gross income shown by the trading statement before the net profit can be ascertained.

667. The cost formula following ¶664 may be further illustrated by the following diagram, in which it will be noted that 100% represents the "total cost," the percentages below representing the proportions of the different elements entering into the total cost and those above representing the additions to find the selling price after providing for selling expenses and profit.



ANOTHER COST FORMULA.

668. The following formula is described as "Analysis of Sale Price of a Manufactured Article."* In this formula it will be seen that there is some difference in the terms used to express the various costs as they are cumulated, "shop charge" being substituted for factory expense, or burden, and "general establishment charge" being substituted for administrative and general expenses, or overhead. In like manner, "works cost" and "inclusive costs" are substituted for factory costs and total costs.



This analysis divides the cost of production into three divisions:

First—The bare cost of material and wages, which is termed prime cost, or "No. 1 cost."

Second—Prime cost, plus the expenses of production incurred in passing through the shops, which is termed works cost, or "No. 2 cost."

Third—Works cost, plus the expenses of the commercial management and selling organization, which is termed inclusive cost, or "No. 3 cost."

The sales price, less inclusive cost, equals the profit on the order. This division of costs agrees with the theory expressed in ¶661, which would, of course, eliminate any part of the general expenses from cost of production.

Note: Other good books for the student of accountancy are:

"Industrial Plants, Their Arrangement and Construction," by Charles Day.

"The Complete Cost-keeper," by H. S. Arnold.

"The Factory Manager," by H. S. Arnold.

"The Depreciation of Factories," by Ewing Matheson.

"Bookkeeping for Accountant Students," by L. R. Dicksee.

"Modern Accounting," by H. C. Hatfield.

* "Expense Burden," by A. Hamilton Church.

SOME OF THE ADVANTAGES OF A COST SYSTEM.

669. When the actual cost of producing a given article or a number of articles or a certain line of goods is known, the manufacturer is in a much better position to manage his business intelligently, either in purchasing materials, in employing labor or in the production of manufactured goods, than he would be without that information. While finding the actual cost of manufacture is the most important object of any cost system, there are many other advantages that are of equal, and frequently of greater importance in the ultimate results produced.

Some of the advantages of a cost system are as follows:

1. To know the exact cost of the materials entering into each manufactured article, order or job, and to have all material purchased and used correctly accounted for, so that the balance shown by the materials account may agree with the inventory value of the materials in the storeroom.

2. To know the amount and the wage value of time spent on each article, operation or order, and to know the degree of efficiency of each workman so that those who are high in efficiency may be rewarded and those who are low may be dispensed with; and, particularly, to assign tasks to each workman in proportion to his skill and ability to perform them well and efficiently.

3. To know the relative cost of production by the use of improved machines over old and less efficient types, and to know the cost per hour or day of operating each machine separately or in groups, departments or producing centers.

4. To know the actual cost of "burden" expenses of the factory or shop, or of "overhead" expenses of the office or administrative department, and of *depreciation* which should be included in the cost of manufacture and distributed over the product.

5. To know the location, the condition and the advancement of each unfinished article, order or contract, at any given time while in the process of manufacture.

6. To know by running book inventories, supported by controlling accounts, how much of each kind of material, supplies, and finished goods is on hand, so that, with the smallest investment of capital, orders may be placed in right quantities and at proper times to meet all requirements, and to prove these accounts at stated intervals by actual inventories of stock on hand.

7. To show on manufacturing, trading and profit and loss statements or on statements supplementing them, all essential elements of cost and production in whatever detail they are desired.

8. To make possible the preparation of statistical and other statements, so arranged that the information contained therein may be compared with similar statements of other fiscal periods to ascertain: (*a*) increase or decrease of total output; (*b*) increase or decrease of monthly output; (*c*) increase or decrease of idle time; (*d*) increase or decrease of labor efficiency and of machinery efficiency; (*e*) increase or decrease of cost of production per order, job or

contract or per any other convenient unit of comparison; (*f*) increase or decrease of selling expenses, of administration expenses, of gross profit and of net profit; (*g*) relative efficiency and cost of different classes of labor.

9. To have such results available as will disclose defects in organization or administration, so that they may be rectified.

10. To know the productive value of every unit or factor available for use in the factory or plant, so that the exact cost of each item entering into the manufacture of any given article or product, and its factory cost, may be correctly and accurately ascertained in estimating the cost and selling price of goods called for in prospective orders, jobs or contracts.

11. To know the percentages or amounts which must be added to factory cost to cover overhead and other expenses necessary to produce and market the goods at a profit, called for in estimating on prospective orders, jobs or contracts, or otherwise.

12. To have information at hand that will provide a basis for calculating the allowances which should be made for unexpected contingencies and losses in estimating the cost of goods called for in prospective orders, jobs or contracts.

669*a*. **Thus it will be seen** that an efficient cost system enables the manufacturer to decrease costs and increase production and profits in many ways which would otherwise be impossible; such as:

1. To reduce the cost of and waste in material and time used.

2. To increase labor production and secure higher efficiency in workmen by assigning maximum tasks which they are willing and competent to perform.

3. To reduce cost and increase production by the use of improved machinery.

4. To reduce expenses in factory or office by increasing the efficiency of employees and dispensing with unnecessary labor and inefficient service.

5. To know the maximum capacity of the factory or plant in a given process, group, department or producing center for a given time, that work may be so distributed as to maintain the factory or plant, as a whole, at the highest point of productive efficiency.

6. To establish wage systems that will secure to the diligent the proper rewards for industry and that will encourage and stimulate workmen to perfect themselves in ability and producing capacity.

7. To know the goods which may be manufactured and sold at the largest profit, and to know those goods which cannot be manufactured and sold at a fair profit, so that the sales of the former may be increased and those of the latter diminished or discontinued.

8. To estimate accurately and expeditiously on specifications of prospective orders or contracts.

670. Many advantages other than those enumerated follow the introduction of well-administered cost systems, although they vary somewhat in importance, depending upon the condition and circumstances of the business. The extent to which increased efficiency in labor, machinery, operation and output is secured by the introduction of a cost system determines, in a large measure, the extent of its usefulness and value in a manufacturing concern.

671. It is not the purpose of cost accounting to show what a given order, job or contract *should* cost or to show its *estimated* cost or to show any cost other than the *actual* cost after it is completed; *i.e.*, the purpose is to show the exact cost of each article made, and, through the various subsidiary and controlling accounts, what the actual results of the manufacturing processes have been. *A comparison* between the estimated cost when the order, job or contract was accepted, and the actual cost when it is completed, will show any inaccuracies in the estimate, and will give substantial information for making future estimates.

672. The efficiency of a cost system depends almost wholly upon the organization back of it and how the system is planned, installed and carried out. The best cost systems are usually those which have small beginnings and are gradually developed and perfected until they fully meet the particular requirements for which they are intended. In planning a cost system, care should be taken to provide for the practical requirements rather than the theoretical requirements of the case, and to avoid the creation of a system that will be expensive to install or operate. It is impossible to formulate or construct a single system of cost accounting that will meet the requirements of every line of business; indeed, a special system must be planned for each particular concern, as no two establishments are likely to present for consideration the same conditions and facts.

673. Before attempting to formulate a cost system for any particular concern, it is first necessary to make a careful study and survey of the plant or factory and its organization, and of all the circumstances surrounding it. However, as the purpose of this book is to give consideration to the accounting features of cost systems rather than to the devising of cost systems or the study of shop organization, management, labor efficiency, etc., these topics receive only incidental attention.

WAGE SYSTEMS.

674. Time is one of the principal and most expensive elements of cost in manufacturing. As labor is one of the elements of prime cost, some discussion of wages is necessary. There are various wage systems in common use, such as the day rate, piece-work rate, differential rate, premium, bonus, profit-sharing, stock distribution or some combination of these systems. The best system to use is determined by the conditions surrounding the particular establishment in which it is to be employed. An understanding of these systems is important to the student of accounts, principally because, in many instances, they form the basis of computation for the distribution of factory expenses, or burden.

The day rate. This is perhaps the commonest method of paying wages. Under this method each workman is paid a certain price for each day's or hour's labor, depending upon his skill and experience.

Piece work. Under this method, each workman is paid a certain price for the production of a certain article or part. He is paid for what he does and no more. It has many advantages, but in its practical operation it has certain deficiencies that, not infrequently, make it objectionable.

Differential rate. This is the piece-work method, modified by an application of the time rate to the work. By this plan the workman is paid "a higher price for quick time and perfect work, and a lower price for slow time and imperfect work." This system is more nearly ideal in its operation than either the day-rate or the piece-work plan.

The premium plan. This method differs from piece work by paying a premium for the completion of a certain task in less time than the average time allotted for its performance.

The bonus plan. This is, practically, a combination of the differential and premium plans, in that it offers "an increase in the hourly wages for the time actually spent, the rate, itself, depending upon the per cent of time gained."

Profit-sharing and stock distribution. These are held out as ideal methods of increasing production and establishing the best relations between employer and employee by having each workman share in the profits in addition to his regular wages. There are various methods suggested for accomplishing this result, but as this plan has not been adopted in many instances, its actual value as a wage system has not been fully determined.

Full descriptions of these and other wage systems are found in the following books, which may be referred to with profit:

"Work, Wages and Profits," by H. L. Gantt.
"Factory Organization and Costs," by J. L. Nicholson.
"Profit-Making Management," by Charles U. Carpenter.
"Efficiency as a Basis for Operation and Wages," by Harrington Emerson.

DISTRIBUTION OF INDIRECT EXPENSES.

675. The factory cost of an article, as previously stated, is made up of three elements of cost—material, labor and factory expenses, material and labor being known as *direct* costs, while factory expenses are known as *indirect* costs or charges.

676 The accurate distribution of factory expenses ("burden" and "overhead") among the different orders, jobs or contracts, so that each article manufactured may be charged with its actual cost, presents perhaps the most difficult problem as well as one of the most important with which the cost accountant has to deal, and its difficulty is increased in proportion to the number of the kinds and varieties of goods manufactured. (¶756)

677. The fixing of a correct basis of distribution or as nearly an exactly correct basis as may be possible, which will connect and identify every item of cost with the particular order, job or contract to which it belongs, so that the actual cost of producing each article may be definitely known, is fundamental in cost accounting. This must be found in some *unit of measurement* that will most nearly assign to each article the exact manufacturing expense which properly belongs to it. If this unit of measurement is uncertain or variable in its application, the cost system must fail to accomplish its most important purpose from the fact that *it will not certainly tell the truth*, no matter how efficient it may be in other directions.

678. Three distinct units of measurement have been used, either singly or in some combination of them, as the basis of distributing factory costs They are "wages value," "wages time," and "machine time." *Wages value* is the total cost of direct labor for a given period. *Wages time* is the total number of hours direct labor is employed for a given period. *Machine time* is the number of hours a given machine or process is in operation within a specified period.

679. Methods of distributing burden and overhead. A number of different methods are used, based upon one or more of these units of measurement, each one doubtless having some advantages over the other under certain conditions. Some are very simple in their practical operation, while others are more complex and intricate. Unfortunately, the simpler methods are seldom accurate under usual manufacturing conditions, while, on the other hand, manufacturers are slow to adopt the more exact and scientific methods because of the greater expense required in their practical operation and maintenance. Several of these methods will now be briefly discussed. Extended discussions may be found in the following publications, from which some of the statements in this chapter are taken:

"Proper Distribution of Expense Burden," by A. Hamilton Church.
"Production Factors," by A. Hamilton Church.

680. Direct labor cost method. This method of distributing burden and overhead (manufacturing) expenses is based on the theory that the product increases in value in proportion to the cost of labor entering into it, and that the greater the amount of labor involved in the process of manufacture the greater the expense required to supervise the labor and to conduct the factory, works or shop, and that, consequently, the burden should be distributed in the proportion the labor employed on a given order, job or contract bears to the total wages paid for the period of time. This method, by reason of its simplicity, is the one most commonly used, although it is very inaccurate under most conditions and is, therefore, likely to gradually disappear as better methods are adopted. *The rate* to be used in distributing the burden by this method is found by dividing the total amount of estimated manufacturing expenses for the period by the total cost of the direct labor for the same period of time. (¶720)

Illustration: Supposing the total estimated factory expense, or burden, is \$780, and the total wages, \$1200, the rate per cent for distributing the burden is \$780 ÷ \$1200 = 65%, *i.e.*, 65% of the value of the labor charged to an order should be added to cover the cost of burden. Thus, an order showing cost of material, \$50, cost of direct labor, \$60, would have added to it 65% of \$60, or \$39 (¶722*c*), giving a total of \$149 as the total factory cost. When an equal percentage has been added to all the orders on which the \$1200 for labor has been charged for the month, it will absorb and take up the total charge against factory expenses of \$780.

681. Direct labor hours method. This method is similar to the direct labor cost method except that the number of productive hours is used as the basis of calculation instead of the total amount of direct wages, *i. e.*, the amount of indirect expenses is divided by *hours* instead of *dollars*. *The rate per hour* to be used is found by dividing the total estimated manufacturing expenses by the number of productive labor hours for the same period of time. Both the labor cost and labor hour method give an *average* result instead of a *direct assignment of the exact cost to the article produced*, and for this reason they are both objectionable.

Illustration: Supposing the \$1200, or the cost of labor, in the preceding illustration, represented 3200 labor hours, then the rate is found by dividing \$800 by 3200, which equals twenty-five cents per labor hour to be added for burden. If 155 labor hours were expended on the preceding job, the amount to be added for burden would be .25 × 155 = \$38.75, making the total cost of the order \$148.75.

682. Direct labor and material method. This method is considered to be more accurate than either of the methods previously described, when the material cost is greater than the labor cost. *The rate* to be used is found by dividing the total estimated factory expenses by the total cost of the material and labor consumed for the same period.

Illustration: If the material used for the month cost $1100, the direct labor cost $750, and the total factory expenses for the month were $975, that amount divided by $1850 would equal 50%, or the rate. If the labor and material on a given order amounted to $116, 50% of that amount, or $58, should be added to cover expense burden.

683. Machine rate method. This method is advocated by quite a number of cost specialists. It is intended to diminish, as much as possible, indirect factory expenses that, under the preceding methods, must be prorated on a more or less arbitrary basis, and to charge them directly to the articles produced; but the method is limited, in the opinion of some writers, to those factories or shops where the majority of operations are machine processes. The plan of procedure under this method provides for charging the labor and all burden or overhead expenses directly to a process or machine, in such a way as to show the total cost per hour or unit of measure of operating the machine or process. This method is substantially as follows:

1. All expenses which can possibly be charged to machines or processes are so charged. This includes indirect labor, supplies, interest, floor space, depreciation, etc., and sometimes superintendence and other general factory expenses are included. It is this step that constitutes the essential essence of this method.

2. The indirect expenses (other than the above) are then prorated and distributed over the machines or processes.

3. Combining the charges of one and two, the total machine rate is determined, which includes all items of cost but material and direct labor.

The rate to be used in distributing the indirect expenses is found by dividing their amount by the total number of operating hours or other unit of measure for the same period of time.

(*a*) To find the cost of any article is then a simple process. The number of hours a given order, job or contract is operated on at each machine or process, multiplied by the machine rate for that process; gives the different process costs. The sum of these, or the total process cost, plus the material and direct labor cost, gives the total factory cost.

Illustration: If the work on a given order was operated on at machine No. 1, for twelve hours, and the rate was thirty cents an hour, the *process cost* at that machine is $3.60. If five hours were required at machine No. 2, on which the rate was forty cents an hour, the process cost at that machine is $2.00. If the work required twenty-four hours at machine No. 3, at the rate of eight cents, the charge would be $1.92. Total process or factory cost, $7.52.

(*b*) The machine rate method would give well-nigh accurate results if all the machines and other processes *were in continuous operation*, but it fails to take account of the *idle time* when part of the machines or processes are not in operation. This is the fatal weakness of the method, as it leaves the proper disposition of those expenses which are continuous in connection with each producing factor unprovided for, with the consequent certainty that accuracy in the distribution of costs has not been attained.

684. Scientific machine rate and supplementary rate method. This is a method which has been devised to overcome the deficiencies and inaccuracies of the other methods described in the preceding paragraphs. In this method, *labor value* and *labor time* are almost entirely eliminated as units of measurement in the distribution of expense burden, while, like the machine rate method, it utilizes the principle of *machine time* as the unit of measurement, but it goes much further by providing for the proper distribution of *idle time.* It regards the shop or factory as a collection of small "production centers," each differing from the other in the cost to operate, but with certain common connecting bonds. By a production center is meant either a machine or a bench at which work is done or it may be an open floor space used for different purposes. These are also designated as "productive factors."

a. Factory expenses, under this plan, instead of being considered as one lump sum, are kept separate, each expense being subdivided and prorated to the various factors of production *in the exact proportion that each factor derives benefit from the expense.* For instance, rent is subdivided and charged to each productive factor in proportion to the floor space it occupies, and so with other items of expense, that is, each production center, or factor is charged with the cost of the different expense elements which enter into the service it renders in production.

b. These elements of cost consist of the rent for the space, power, light, heat, insurance, interest, depreciation, repairs and maintenance, and all other items of expenditure necessary in the operation of a particular productive center for a given period of time. The sum of these items for a given period, say a month or a year, gives the total cost of operating and maintaining that particular productive center for that time and, consequently, represents the cost of the service it renders as one of the productive factors of the establishment. This sum, divided by the number of working hours in the period, will give the *cost per hour* of the service rendered by that productive factor in the manufacturing processes of the establishment.

c. One of the objects of this method is to change practically all of the ordinary factory expenses represented in these elements of cost from *indirect* to *direct* charges by connecting them with and including them directly in the cost of operating a particular machine or productive center. Since by this method each productive factor, or center, is charged with its share of the different elements of cost, it disposes of all factory expense by absorbing them in the hourly machine rate charged against the articles in process of manufacture, except those expenses which are of such a general character that they cannot be identified with any particular order or job, such as idle machine or productive factor time, waste time, spoiled work, superintendence, etc., all of which are provided for in a "supplementary rate," described in paragraph 684*h*.

d. The product of a shop or factory in which all the productive factors are at work represents its *capacity for manufacture.* When part of the productive factors are idle, those in operation represent the *utilized capacity* of the shop or factory, while those which are idle represent the *wasted capacity. Idle machine time,* or waste time, as it is frequently designated, is, therefore, the amount of time the various productive factors are not in operation, *i.e.,* the time they are unemployed.

e. Many of the elements of cost attaching to each productive factor go on whether the factor is in service or not, such as rent, insurance, light, heat, interest, depreciation, etc. The idle time of a productive factor, therefore, represents a loss equal to the cost of the various elements of expense charged to that factor, and if the profit earned by those productive factors which are in operation is to be saved, this loss must be met by adding its equivalent to the cost of the goods in course of manufacture, which, of course, will increase the normal cost of these goods, the normal cost being the cost when all the productive factors are employed.

f. This added cost on the normal cost, while it may be distributed over the cost of goods in course of manufacture, is, strictly speaking, no part of such cost and merely shows the ratio of *wasted* capacity to *utilized* capacity, and separates from the normal cost a part of the actual cost of production which would otherwise be concealed.

g. Wasted capacity adds to the production cost of the articles in process of manufacture in the inverse ratio of wasted capacity to the total capacity of the shop or factory; for instance, if a shop is running at one-half its normal capacity, it will practically double the cost of production, outside of direct labor and material, in those parts of the shop that are in operation, while, if the shop is running at one-fourth its normal capacity, it will practically increase the cost of production to four times the normal cost.

h. The supplementary rate, referred to in the heading to this paragraph (¶684), takes care of the *undistributed* balance of factory expenses due to idleness of productive factors and waste time, also of spoiled work, superintendence or supervision, and such other elements of cost as are not distributed through the established hourly machine rate for each productive factor. The amount of these expense charges to be distributed through the supplementary rate is found by deducting the total amount of the charges against work in process, for services rendered by productive factors in the manufacturing processes of the period, from the total manufacturing expenses, the difference being the amount to be distributed through the supplementary rate; *i.e.,* the total manufacturing expenses, less the total value of the productive machine hours for the same period, equals the amount to be distributed by the supplementary rate. (¶721*b*)

i. The supplementary rate is found either by considering it as an additional hourly burden charge placed upon each producing factor contributing to the work performed in the period, or it may be reduced to a percentage of increase on the amount already distributed by the machine rate.

Illustration: Supposing it is found that factory expense account was charged during the month with items amounting to $170.75. Machine No. 1 worked 140 hours at 30¢ = $42 for the month; machine No. 2 worked 150 hours at 25¢ = $37.50 for the month; machine No. 3 worked 260 hours at 20¢ = $52 for the month; machine No. 4 worked 175 hours at 10¢ = $17.50. Total hours, 725; total amount distributed, $149. The total charge to factory expense, $170.75, less the amount distributed, $149, equals $21.75 yet to be distributed. This is the amount which is to be distributed through the supplementary rate by either one of two methods.

It may be treated as an *hourly burden,* the amount to be added to each productive hour, which is found by dividing $21.75 by 725, or 3¢ per hour, which should then be added to the hourly machine rate on each article manufactured during the month; for instance, the rate for machine No. 1 would be 43¢ instead of 40¢.

Or the balance, $21.75, may be reduced to a *percentage* of the amount already distributed; thus, $21.75 ÷ 149, the expense burden already distributed, = 14½%. Therefore, if the machine rate charge against a given order was $25, 14½% of that amount, or $3.63, would be added, making a total of $28.63. Under this latter plan, the calculation is reduced to a very simple matter.

It will be seen that by either method the supplementary rate is very easily disposed of, and where the operations of a given shop or factory continue in a fair ratio of regularity, either the increased hourly rate for each productive factor or the increased percentage on the total machine rate charge may be added to each order. Where there is a considerable variation in the time the productive factors are employed in different months or in the unproductive or waste hours, it is necessary to establish a separate rate for each month either in the form of an hourly machine charge or a percentage of the total machine charges against each order.

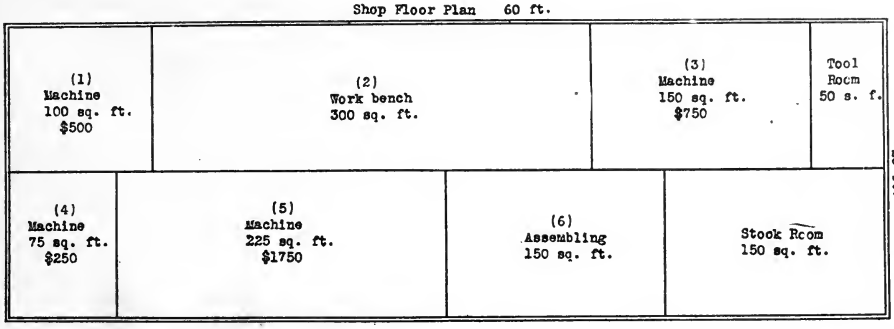
j. The scientific machine rate and supplementary rate method is ably presented and discussed by A. Hamilton Church (see ¶679), and as it is the most nearly scientific method yet discovered, it is worthy of careful study and consideration. It rests on the principle that *organization* is the fundamental basis of satisfactory cost records, and that the best system of costs cannot do more than give the results which naturally follow the kind of organization in force, whether good or poor, and that, consequently, the most satisfactory results can be secured only through the most *efficient* organization.

685. Organization, in a manufacturing sense, is defined as being the ways and means adopted and followed to secure *efficient production*, while the true object of cost accounts is to register and record every stage and step of production as it actually happened, with the natural consequence that when deficiencies in organization are discovered, they may be corrected: so that organization and cost accounting are co-operative, one benefiting the other, both of them being of the highest importance in the economical production of manufactured goods.

685*a*. Distribution of Costs. The illustration on the opposite page shows the method for assigning to each productive factor its proportion of the different cost elements of factory expense. In the illustration, but six producing factors are shown. In many factories, shops or works there may be a hundred or more such productive factors in the various departments, but the method of ascertaining the cost of each productive factor is the same whether there are few or many. In the illustration it will be noted that four of the productive factors are machines, the fifth is a workman's bench for hand work, and the sixth is a vacant space used for assembling parts and other similar purposes.

ILLUSTRATION 102

Shop Floor Plan 60 ft.



Explanation: This floor plan shows a space 60 feet long and 20 feet wide, or 1200 square feet. The tool room and stock-room occupy 200 square feet, leaving 1000 square feet occupied by the six productive factors. The number of square feet occupied by each factor is shown. The value of each machine is also shown, taken from the inventory, at cost price. The same method of procedure would apply to any other space or number of floors occupied for factory purposes.

ILLUSTRATION 102*a*

ESTIMATE OF MANUFACTURING EXPENSES FOR THE YEAR BEGINNING JAN. 1, 19 (PAR. 720, 752)

Rent of factory space, 60 x 20 ft.	800.
Light and heat (per cost of previous year)	50.
Power (4 machines, per meter record for last year)	375.
Taxes (per last year's assessment)	45.
Insurance on plant	65.
Repairs and renewals on machines (estimated on previous expenditures)	750.
Supplies, oils, etc.	75.
Depreciation and interest on plant	420.
Tool room charges for repairs, etc.	150.
Superintendence	900.
Incidental labor	420.
Overhead management and expense	400.
	4450.
Monthly average (4450 ÷ 12)	370.83
Hourly average (based on 2700 working hours in year)	.16 1/2

(*a*) *Illustration 102a* shows the estimate of manufacturing expenses made up at the beginning of the fiscal period (¶ 720) as it would appear in the manufacturing expense estimate book. (¶752)

(*b*) *Illustration 102b* shows the distribution of these expenses to the various productive factors or centers, with the yearly, monthly, and hourly cost of operating each factor. It will be seen that the items for rent, light and heat, and taxes are distributed in the proportion of the number of square feet occupied by each factor to the total number of square feet (1000) occupied by all of the factors. Power is usually distributed in the proportion of the horse-power of each machine to the total horse-power used, although when electricity is the power and each factor has its own dynamo, this charge may be accurately ascertained by a separate meter for each machine. Insurance, repairs and renewals, supplies, oils, etc., depreciation and interest, tool repairs, superintendence, and incidental labor are distributed by special determination of the proper cost to be allotted to each factor; for instance, insurance is usually allot-

ILLUSTRATION 102*b*

DISTRIBUTION OF ESTIMATED MANUFACTURING EXPENSES FOR YEAR 19 . SHOWING OPERATING COST OF EACH PRODUCTIVE FACTOR FOR THE PERIOD.

Items	Total	Productive factors 1.	2.	3.	4.	5.	6.
Rent	800.	80.	240.	120.	60.	180.	120.
Light and heat	50.	5.	15.	7.50	3.75	11.25	7.50
Power	375.	41.75		93.	26.60	213.65	
Taxes	45.	4.50	13.50	6.75	3.38	10.12	6.75
Insurance	65.	10.		15.	5.	35.	
Repairs and renewals	750.	41.66	83.33	166.67	125.	291.67	41.67
Supplies, oils, etc.	75.	3.50	5.	30.	5.	25.	6.50
Depreciation and Interest	420.	160.		60.	70.	130.	
Tool repairs, etc.	150.	25.	12.50	37.50	18.75	56.25	
Superintendence	900.	60.	300.	60.	60.	180.	240.
Incidental labor, helpers, etc.	420.	21.	52.50	21.	10.50	105.	210.
Overhead expenses	400.	66.67	66.67	66.67	66.66	66.67	66.66
Yearly cost	4450.	519.08	788.50	684.09	454.64	1304.61	699.08
Average monthly cost	370.83+	43.27+	65.75	57.-	37.89	108.72-	58.26-
Hourly cost, basis of 2700 working hours per year	1.65-	.19+	.29+	.25+	17+	.48+	.25+

ted to each factor in the proportion of the value of that factor to the total value of the factors insured. Repairs and renewals must necessarily be allotted to each factor in proportion to the cost of maintaining that factor, based upon previous experience or costs. The same is true of supplies, oils, etc., and tool repairs. Depreciation and interest are figured upon a certain percentage of the cost of each machine and other depreciable equipment. The expense of superintendence and incidental labor is distributed in the proportion of the total time that each factor requires in its operation. Overhead expenses are usually distributed equally over the various factors, but they may be distributed in different proportions where any part of this expense can be properly allocated to a particular factor or factors.

(*c*) The hourly machine rate for each factor shown on the statement is the cost of operating that factor. (¶ 684*d*) When part of the factors are idle, idle time and other cost elements do not increase the production cost of those factors which are in operation, but they do increase the production cost of the factory, *i. e.*, each article will cost more to make.

(*d*) On the statement showing the distribution of the estimated manufacturing expenses for the year, the average monthly and hourly operating cost of each factor is shown. This is known as the "production cost" of each factor, to which must be added such additional costs, determined through the supplementary rate, as will cover the loss from unproductive factors and other sources to find the hourly charge for work performed on any order or job by each productive factor. (¶ 684*i*)

(*e*) When the cost of operating any particular productive factor increases or decreases because of unexpected or contingent circumstances, the monthly and also the hourly production cost should be increased or decreased accordingly.

To illustrate, the hourly production cost of factor No. 1 is shown in the statement to be 19¢. Supposing an additional charge of 7 cents per hour, determined by the supplementary rate, is necessary to cover the cost of idle factors, etc., the hourly charge for factor No. 1 is 26¢. When more productive factors are in operation, this hourly rate for machine No. 1 would be lowered. When fewer factors are in operation, it would be increased, and the same would be true of all the factors. If any of the elements of cost in the estimate of manufacturing expenses for the period are increased or diminished, corrections should be made in the hourly production cost of each factor accordingly.

METHODS AND SYSTEMS IN MANUFACTURING ACCOUNTS.

686. Methods and systems of conducting manufacturing accounts vary greatly, depending upon the nature and extent of the business conducted, and more particularly upon the *units of information* which the accounts are intended to supply.

687. There are two principal methods of conducting manufacturing accounts, one which may be designated as the "department" method and the other as the "cost" method.

688 In the department method, the accounts are planned to show the cost of operating an entire shop or factory, or some department of it, including the cost of the labor and the various materials and expenses, the object being to show the *gross manufacturing cost of the shop, factory or department* for a given period and, finally, the gross profit on the manufactured goods sold.

689. In the cost method, the accounts are planned to show the manufacturing or production cost of the articles called for in a particular order, job or contract, without reference to the profit of a particular shop or department, the object being to show the *total cost of each order, job or contract* and, finally, the gross profit between cost and selling price.

690. It is not impossible to construct a system of accounts that will show both department and cost accounts in the same set of books; indeed, in the books of many of the best organized manufacturing concerns, where the product is at all varied in its character, the books are kept to show the results of both methods.

THE DEPARTMENT METHOD OF MANUFACTURING ACCOUNTS.

691. When the department method is followed, which has for its unit of consideration the plant, factory or department, if it is desired to show only the gross cost and the gross profit derived therefrom for the period, it is necessary to open a single account, only which is debited for all costs, including materials, labor and expenses. If it is desired to know the separate costs of the materials, labor and expenses, an account should be kept with each. If there are several materials, various expenses or other elements of cost entering into the finished product, and it is desired to know the cost of each, separate account should be kept with them or they should be separated on analysis sheets before the manufacturing statement is prepared.

692. Manufacturing accounts of this description are in all essential particulars similar to the ordinary trading accounts, and when kept in connection with the proper sales accounts, the gross profit of a plant, factory, shop or department can be readily and accurately ascertained. By opening the necessary accounts, the manufacturing statements can be made to show the results of the transactions for the period in whatever detail is desired. Where accounts are kept for a number of departments in the same establishment, they closely resemble the accounts of a department store in a trading business.

693. When the department method of conducting manufacturing accounts is followed, it is frequently supplemented by cost sheets and other memorandums which are depended upon for figuring the costs and the selling prices of the different articles manufactured. In many instances fairly efficient cost systems are thus maintained.

Rules for Debiting and Crediting Manufacturing Accounts when the Department Method is Followed.

694. The following rules are for accounts opened under the department plan, where the balances shown by the various material, labor and expense accounts, after being credited with inventories, *represent the various elements of cost that enter into and make up the total manufacturing cost.* These accounts and the rules therefor should not be confused with those given when the *cost method* is followed.

Rule for Debiting and Crediting Material Accounts When Kept to Show the Cost of Material Used.

695*a*. *Debit* material accounts, under proper headings, for costs of all material purchased, including freight, drayage, and all other charges necessary to place the material in the factory ready for use.

b. *Credit* material accounts for all deductions from cost, and *at cost price* for all materials previously charged to this account which are sold or otherwise disposed of.

c. *The balance*, less the inventory of materials on hand taken at cost, shows the cost of the material *used up* in the goods manufactured for the period.

696. Pay-roll and time cards. A time card is usually provided for each workman in an establishment on which a record is kept of his time and the purpose for which it was employed. From these time cards the pay-roll and pay-roll distribution sheets are made up. There are many different forms of both time cards and pay-rolls. A pay-roll is not infrequently bound in book form, and is sometimes combined with a form of time card. In other instances the time shown

by time cards is recorded in a time book, from which the pay-roll is later made up. The proper design of these cards and books is determined by the requirements of the particular business for which they are intended, and by the kind of mechanical time-recording system used if such a system is employed.

RULE FOR DEBITING AND CREDITING LABOR ACCOUNTS WHEN KEPT TO SHOW THE COST OF LABOR EMPLOYED IN A GIVEN SHOP, FACTORY OR DEPARTMENT.

697*a*. *Debit* labor account for the cost of all labor employed in manufacturing the goods of a shop, factory or department for the period.

b. *Credit* the account for the value of any labor employed elsewhere which is charged to this account.

c. *The balance* shows the cost of the labor employed in manufacturing the goods of the shop, factory or department for the period.

d. NOTE—The labor account described above must not be confused with the labor account described in ¶563. That account is really an adjusting account between the pay-roll and the various accounts to which the cost of labor is finally charged, and should be opened under the title of "pay-roll" account when kept in connection with the account described above.

698. Manufacturing expenses. These expenses are described in ¶685.

699. RULE FOR DEBITING AND CREDITING MANUFACTURING EXPENSE ACCOUNTS.

a. *Debit* manufacturing expenses, under proper headings, for the cost of all expenses incurred in operating the shop, factory or department.

b. *Credit* the account for any returns from expense items charged to the account.

c. *The balance* shows the cost of the expenses incurred in connection with the manufacture of the goods of the shop, factory or department for the period.

THE COST METHOD OF MANUFACTURING ACCOUNTS.

700. When the cost method is followed, which has for its unit of consideration *the manufacturing cost of the articles called for in each order, job or contract,* it is necessary to devise a system of cost records and accounts that will show in detail the elements of cost entering into each order, job or contract from the time it is begun until it is completed. Such a system differs in many important particulars from a system that would meet the requirements when the department method alone is followed, notably in the treatment of material, labor and expense accounts, and especially if the cost records and accounts are to be supported by controlling accounts in the general ledger.

701. The cost method of accounts is associated with and is the necessary complement of what is popularly termed "cost accounting," which is, speaking more accurately, cost *finding* and cost *distributing*, and is, therefore, as much a question of shop management and a proper analysis of shop conditions and records as it is of pure bookkeeping. This important subject is treated in a separate chapter, beginning with ¶647.

702. The principal manufacturing accounts, under the cost method, are designed with the double purpose of showing costs of materials, labor, manufacturing expenses, etc., and of acting as control accounts for inventories and the various supplementary accounts in the factory books. These accounts are given various names by different accountants, but in this text they are designated as "materials" account (¶704), "materials in process" account (¶710), "productive labor" account (¶714), "manufacturing expense," or "factors expense"account (¶719), "factory expenses" account (¶732), "finished goods" account (¶740), "sales" account (¶745), and "cost of goods sold" account (¶745). "Idle productive factors" account is an account that is sometimes kept, which is debited for idle time of productive factors ascertained from daily reports of idle machine hours, and is credited for the same amount when the idle time is distributed over work in process through the supplementary rate. This account would, therefore, show in one item, monthly, the lost time, or, more properly the *lost efficiency* of the works or shop; but the same result may be ascertained in another way, as is described in ¶724. This account is not shown in this text.

MANUFACTURING ACCOUNTS WHEN THE COST METHOD IS FOLLOWED.

703. A comparison of the following rules with those given for manufacturing accounts when the department method is followed, will show a number of important differences, and care should be exercised not to confuse them. (¶694)

704. Materials, under the cost method of accounts, include all materials of every kind and description purchased to be used in the manufacture of the articles for which the concern is conducted. Many accountants class materials under the head of "stores" to distinguish them from "stock" which is used to designate finished manufactured goods. Usually but one "materials" account is necessary, whether one or more manufacturing departments are maintained, except where separate groups of accounts are kept for each department. Materials account controls the stores, or stock ledger. (¶708)

Rule for Debiting and Crediting Materials Account When the Cost Method is Followed.

705. Debit "materials" account,—

a. For the cost of all materials purchased which enter directly into the goods manufactured, including freight, drayage, and all other charges necessary to place the materials in the stock-room ready for use, as per invoice, or purchases journal or vouchers payable register. (¶747)

b. For all materials returned to the stockroom from work in process which had been credited previously to this account, as shown on "stores returned" blanks, per transfer inward journal. (¶749)

706. Credit "materials" account,—

c. For all materials taken from the stockroom on requisition for work in process, called for on requisition blanks, per transfer outward journal, *at cost.* (¶748)

d. For all materials taken from the stockroom on requisition, when disposed of by sale or otherwise than for work in process, at cost per transfer outward journal.

707. The balance of the account shows *the cost of the materials on hand,* which should equal the value of the stock on hand shown by inventory and by the material, or stock ledger.

708. Material, stock, or stores ledger. This is a subordinate ledger, usually kept by the stock clerk, of which the materials account in the general ledger described above is the controlling account, in which a record is kept of all materials purchased and of all materials issued upon requisition. Under appropriate headings, accounts are opened for each kind of material, the number and cost price of the items received being entered on the debit side, and the number of items and cost price of the materials issued upon requisition being entered on the credit side. The difference between the *number* of items of each kind received and issued must equal the number of items on hand in the stockroom, and the difference between the *cost price* of the materials purchased and the cost price of the materials issued on requisition must equal the balance shown by the materials account in the general ledger. Thus, it will be seen, two checks are had—one from the general ledger and another from the inventory. This ledger may also be used when the department method is followed. It receives its entries for the debit items from the invoice, or purchases journal, and from the transfer inward journal. (¶747, 749) Credits come from the transfer outward journal.

Work in Process.

709. **"Work in process"** is a term used in manufacturing establishments to indicate all articles in process of manufacture. It covers materials and direct labor required for the work in process, as well as manufacturing expenses, from the time the materials are received from the store-room until the time the finished articles called for in the order, job or contract are delivered to the warehouse, sales-room or shipping department. "Work in process," therefore, involves three accounts—"materials in process" account, "labor" account and "manufacturing expenses" account.

Materials in Process.

710. **"Materials in process"** refers to the materials in the work-shop as distinguished from the materials in the store-room. In this account is recorded the cost of the materials used in the orders, jobs or contracts in process which, with the cost of the labor, makes up the prime cost of the goods manufactured.

Rule for Debiting and Crediting "Materials in Process" Account When the Cost Method is Followed.

711. Debit "materials in process" account,—

a. For all materials received from the stock-room on requisition, at cost price, as shown by requisition orders per the transfer outward journal. (¶748)

712. Credit "materials in process" account,—

b. For all materials returned to the stock-room, at cost price, which were previously debited to this account, as shown on "stock returned" cards per the transfer inward journal. (¶749)

c. For the cost of materials used on each order, job or contract when completed and the finished goods are ready for sale or delivery or have been placed in warehouse, as shown by "factory cost" cards or job ledger per the finished goods journal. (¶750)

713. **The balance** of the account shows the cost of the materials in the uncompleted work in process, and should equal the sum of the charges for materials on the shop cards or job ledger for all uncompleted orders, jobs or contracts; *i.e.*, it should equal the inventory, and the account should balance after the inventory is entered. (¶754b) This account, therefore, controls the charges for materials on cost cards and requires that all materials received from the stock-room shall be accounted for.

Labor.

714. Labor, under the cost method of accounts, is usually understood to refer to the labor which is employed directly in the manufacture of a particular order, job or contract. This is known as *direct** labor, to distinguish it from *indirect* labor, which is a part of factory expense and will be described under factory expense account. It is the labor which, added to cost of materials, gives the prime cost. (¶664) The account is kept under the head of "labor," or "productive labor" account, and should be distinguished from accounts under similar names described in ¶563 and ¶697.

715. Pay-roll and time cards. These are described in ¶696. The time of each workman is kept by the foreman or, in large establishments, by a time clerk, although in some concerns the workman himself makes the record of his time and the purpose for which it was expended, in which case the time card should be O.K.'d by his foreman. It is from the time cards that the time expended on each order, job or contract is entered on the cost card or in the job ledger, whichever is kept, and it is from the same cards that the pay-roll is made up, usually weekly or monthly, or as frequently as the workmen are paid.

Rule for Debiting and Crediting Productive, or Direct Labor Account When the Cost Method is Followed.

716. Debit "labor" account,—

a. For all sums paid to workmen, in cash or its equivalent, for direct labor, as shown by the pay-roll or time cards.

717. Credit "labor" account,—

b. For all direct labor expended on goods completed, manufactured during the period, as shown by the factory cost cards, per the finished goods journal.

718. The balance of the account shows the amount of labor which has been expended on uncompleted work in process, which should equal the sum of the items for direct labor on the cost cards of uncompleted work, *i.e.*, should equal the present inventory. (¶754*c*) This account, therefore, controls the charges for direct labor on the cost cards, and requires that all time charged on the pay-roll be accounted for.

**Direct* labor is so named because it is expended directly on a particular article or job. *Indirect* labor, on the other hand, is labor that is general in its character and cannot be connected with any particular article or job, such as cleaning shop, distributing tools, etc.

Manufacturing Expenses.

719. "Manufacturing expenses" is a term used to designate the actual expenses chargeable against work in process on shop cards while the work is going through the work-shop in course of manufacture or when completed, to distinguish them from factory expenses, which are included in a general account described in ¶732. When the "scientific machine rate," the "productive factor," or the "productive center" method is used for the distribution of manufacturing expenses (burden and overhead), this account may be designated under the title of "factors expense" account. When any one of these methods is used, the hourly machine or productive factor charges are usually made concurrently on cost cards with the charges for materials and labor, and when added to cost of materials and labor give the *factory cost* or *cost of production.* (¶664) When other methods for distributing manufacturing expenses are employed, they are not charged to the order, job or contract until it has been completed and the total labor time, labor cost or material cost has been determined.

720. Estimates of manufacturing expenses, *usually based upon the cost of these expenses for previous periods,* are required to ascertain the amount of these expenses which is to be distributed for the present period. Such an estimate is known as a *schedule* or *inventory of expenditures,* and is usually made up at the beginning of each succeeding period. It is frequently designated as the "manufacturing expense budget," and is made up of all the various burden and overhead expenses which are to be included in the cost of manufacture and distributed over the various jobs, orders or contracts for the period. When the estimated manufacturing expenses for a given period have been determined, they are then divided by the number of monthly periods included in the estimate. (¶752)

Rule for Debiting and Crediting Manufacturing, or Factors Expense Account.

721. Debit "manufacturing," or "factors" expense account,—

a. For the estimated amount of manufacturing expenses, at cost, for the week, month or other period, per schedule at commencement of period. (¶720, 752)

b. For such an amount as will meet the deficit caused by an *under-estimate* of expenses for the period or for the amount necessary to provide for the *supplementary* rate to be charged to work in process. (¶684*h*,*i*)

722. Credit "manufacturing," or "factors" expense account,—

c. For the amount of manufacturing expenses, at cost, distributed and charged to orders, jobs or contracts as they are in process or when completed during the period, as shown by factory cost cards, per finished goods journal. (¶750)

d. For such an amount as will equal an overcharge to the account caused by an *over-estimate* of the expenses for the period, transferred to following period.

723. The balance of the account, shows the cost of the manufacturing expenses that have been charged or are yet to be charged on the cost cards of the various unfinished orders, jobs or contracts, at the close of the period, *i.e.*, it should equal the inventory of this account. (¶754*d*) Any difference between the balance of the account and the inventory will show an over- or under-estimate of manufacturing expenses for the period—an over-estimate if the balance is the larger, an under-estimate if the inventory is the larger.

723*a*. *Items ¶721a, b, may be* and frequently are omitted by omitting the entry from the manufacturing expense estimate book debiting manufacturing or factors expense account and crediting factory expense account for the estimated expenses for the month or other period. (Read ¶752)

723*b*. *If the entries required for ¶721a, b, are omitted* the balance will then show the cost of the factory expenses distributed for the period. This balance should substantially equal the balance shown by its contra account, "factory expense" account, described in ¶736, when the items called for in ¶735*d* are omitted. Any difference would show over- or under-distribution of manufacturing expenses, described in ¶723.

724. If manufacturing expenses are distributed through hourly machine, productive factor, or productive center time, in which case the account should be kept under the title of "Factors Expense" (¶719), the balance of the account will include the value of the idle, or unproductive time of machine factors or centers, unless the idle time has been distributed monthly in the supplementary rate. This idle time may be accounted for by a daily shop record of the idle time of each machine, factor or center, in a separate book kept for that purpose, which should be totaled for the month. This total is an unfailing barometer of the productive efficiency of the plant. (¶684*h*) The difference between this total and the balance (inventory) of the account will show that part of the manufacturing expenses coming from other sources than idle time which is yet to be distributed.

725. Under-estimates of manufacturing expenses (¶721*b*) must be distributed as a *supplemeniary* charge over the work in process for the period, or it may be carried into the next period, with a corresponding increase of the charges on the goods manufactured in that period; otherwise, they represent a dead loss to the concern. Over-estimates, on the other hand (¶722*d*), have the advantage of creating a reserve, which can be carried forward to subsequent periods, with corresponding reductions in the charges against the goods then in process of manufacture. Either extreme should be avoided, if possible. (¶684*h*, *i*)

Manufacturing Account.

726. The three preceding accounts, viz., "materials in process," "productive labor," and "manufacturing expense" accounts, may be combined and kept as one account, under the title of "manufacturing account," in which case the various elements of cost shown in the separate accounts may be ascertained from an analysis sheet made up from the single account. The accounts are kept separately to provide control accounts that will give an absolute check upon the records kept of material, labor and expenses of the factory, and to guard against loss of materials through neglect to charge them or by theft, for loss of labor time through neglect to charge or caused by idleness of workmen, and to quickly discover inaccuracies in prorating burden and overhead expenses.

Rule for Debiting and Crediting Manufacturing Account, Combining Materials in Process, Productive Labor and Manufacturing Expenses.

727. Debit "manufacturing" account,—

a. For cost of all materials. (¶711*a*)

b. For cost of all direct labor.

c. For estimated cost of manufacturing expenses for the period. (¶721*a*)

d. For cost of manufacturing expenses distributed through the supplementary rate. (¶721*b*)

728. Credit "manufacturing" account,—

e. For cost of materials returned to stockroom. (¶712*b*)

f. For cost of materials in finished goods. (¶712*c*)

g. For cost of direct labor in finished goods. (¶717*b*)

h. For cost of manufacturing expenses charged to finished goods. (¶722*c*)

i. *The balance* of this account consists of: (*a*) the cost of the materials in process of manufacture (¶713); (*b*) the cost of direct labor expended on uncompleted work in process (¶718); and (*c*) the cost of manufacturing expenses charged or to be charged to work in process. (¶723)

729. The balance shows the cost of materials, productive labor and manufacturing expenses included in the work in process not completed. If manufacturing expenses are distributed through hourly machine, productive factor, or productive center time, the balance will include the value of unproductive machine hours, factors, or centers. (¶724)

730. When the estimated manufacturing expenses are not charged to this account (¶727*c*), the balance of the account will show the amount of manufacturing expenses distributed, including the value of idle machine time, although the balance may also contain inaccuracies relating to the materials and labor, which would be revealed only through an analysis of the account, which would virtually separate it into the three accounts indicated.

731. Shop cards and job ledger. Shop cards accompany each order, job or contract during the time the work is in process, and receive entries for all items of material, labor and other direct charges that belong to the work called for on the cards, and also for the charges covering burden and overhead expenses when these costs are recorded concurrently with the charges for materials and labor. On small jobs, these cards are frequently bound in loose-leaf style or indexed by one of the many card systems. Where there are many items entering into the cost of the product it is necessary to keep a job ledger, for which the loose-leaf ledger form is usually preferred. In any event, the card or ledger account finally shows the total cost of materials, labor and other direct charges entering into the cost of the finished product, and also the cost of burden and overhead expenses whether charged concurrently with materials and labor by the machine rate method or not. There are many forms of ruling and arrangement for the cards and stock ledger accounts, the design being determined by the organization of the shop processes and the system of accounts. Shop cards and job ledgers may also be used when the department method of conducting manufacturing accounts is followed.

Factory or Shop Expenses.

732. These expenses are described and the principal items enumerated in ¶645, page 201. It should be noted that they do not include either material or direct labor, which are charged to their own accounts, but that they do include incidental labor and supplies, as well as all other items of factory expense which enter into the cost of production. (Read ¶657, ¶658) While a single expense account is usually kept for factory expenses, they may be classified to any extent desired by opening separate accounts for each class of items, or they may be classified on an analysis sheet, either monthly or at the close of the fiscal period.

733. A sharp distinction should be made between *factory* expense account, here described, and *manufacturing*, or *factors* expense account, described in ¶719 to ¶725. Factory expense account receives the charges for the current expenses of the factory, shop or works, and it corresponds in principle with the general expense account, described in ¶310 to ¶324, while manufacturing, or factors expense account shows *these expenses distributed over the manufactured product;* consequently it will be seen that the items debited to factory expense account are finally credits to the manufacturing, or factors expense account. All items credited to manufacturing expense account in the finished goods journal (¶750) might be credited directly to factory expense account, but it would have the result of confusing such items with credits in the account from other sources, and besides, it would make factory expense account show two results instead of one, which is always objectionable and in opposition to one of the well-established rules of accountancy.

Rule for Debiting and Crediting Factory Expenses.

734. Debit "factory expenses," under appropriate headings,—

a. For the cost of all indirect labor and supplies entering into the cost of goods manufactured.

b. For the cost of rent, fuel and light, power, taxes, insurance, maintenance, repairs and renewals, depreciation, and such other expenses as are incurred in carrying on the work of the shop or factory.

735. Credit "factory expenses," under appropriate headings,—

c. For any deductions or rebates from items charged to this account.

d. For the estimated amount of "manufacturing," or "factors" expenses for a given period, charged to those accounts when they are kept. (¶721*a*)

e. For expense items previously charged to this account transferred to other accounts.

736. The balance (or the sum of the balances if more than one account is opened), shows the over- or under-distribution of manufacturing, or factors expenses. (¶724, ¶725) *If items in ¶735d are not* credited to this account (read ¶723*b*), then the balance of this account should substantially equal the balance shown by its contra account, the manufacturing, or factors expense account (¶721, ¶722), the difference between the balances showing the over or under-distribution of factory expenses.

737. Each factory expense account in a cost system is usually accompanied by a complementary or contra account, which shows the debit items of one account as the credit items of the other, as indicated in the preceding paragraph. For instance, manufacturing, or factors expense account is the *contra* account to factory expense account and is, therefore, an *offset* account to it. As has already been suggested, the transfer entry between these accounts may be omitted, in which case the balances should practically cancel each other.

738. Prorating and distributing general and administrative expenses. Apart from and in addition to factory expenses, or burden, which with the cost of material and labor, gives the total factory cost (see formula ¶664), there are usually certain other items of expense incurred known as overhead expenses. (Read ¶654, ¶658) These overhead expenses must not be confused with the regular administrative and general expenses incurred in the general or financial management of the concern, and which correspond in every particular with those of a trading business, as set forth in ¶297, ¶301, ¶302, ¶310, ¶314 and ¶315; and it should be noted, also, that they rarely comprise more than a small proportion of the items charged to the administrative and general expense accounts, and that in all instances where it is possible, they should be charged directly to the factory expense account and should never appear in the general or administrative expense accounts, in which case, of course, their consideration as separate items in the distribution of expense is unnecessary. (Read ¶658 to ¶663)

739. When factory expenses are charged in general, or administrative expense accounts, or when some proportion of general or administrative expenses are to be included as part of the cost of production of goods manufactured, their amount should be ascertained and included in the schedule, or inventory, of manufacturing expenses for the period. (¶720) When it is desired to show separately such general or administrative expense items as have been thus distributed, it is necessary to open *contra* accounts similar to the contra account for the factory expense account or, preferably, they should be listed separately and charged by journal entry to the factory expense account and credited to the proper general or administrative expense account.

740. Manufactured goods consist of the articles which have been completed and delivered ready for sale to the shipping department or for storage in the warehouse. An account with manufactured goods is kept under the title of "Finished Goods" (usually abbreviated to "Fin. Goods") or "Manufactured Goods."

Rule for Debiting and Crediting Finished Goods Account.

741. Debit "finished goods" account,—

a. For the cost of goods manufactured during the period, at cost of production, *i.e.*, cost of materials, labor and manufacturing expense (burden and overhead), as shown on cost cards for each order, job or contract when completed, per finished goods journal. (¶750)

742. Credit "finished goods" account,—

b. For the cost of goods sold for the month or other period, per "cost of sales" record, stock delivery orders, etc., per stock deliveries journal. (¶751)

c. *The inventory* consists of the finished goods on hand, at cost.

743. The balance of the account equals *the total cost, or inventory value of the manufactured goods in stock*, as shown by inventory or by the stock ledger, when kept. This account, therefore, controls the finished goods, or stock ledger. The total footing of the account for the year or other period, after the inventory for the previous period has been deducted, shows the total cost of the goods manufactured for the period.

744. After the process of manufacture has been completed and the finished goods have been charged to that account, cost of production ends (¶664) and selling, administrative and general expenses begin. It is, therefore, at this point that the manufacturing statement ends and the trading statement begins. The connection between the manufacturing accounts and the trading accounts is through the entry debiting cost of sales account for the cost of the goods sold and crediting finished goods account. mentioned in ¶742*b*

745. "Cost of goods sold," or "cost of sales" account is debited for the cost of the manufactured goods sold. It is an offset, or contra account, to the sales account, the difference between them showing the trading profit for the period. The debit to this account is invariably the credit to finished goods account, as previously stated. Its only purpose is to eliminate the cost of goods sold from the sales account, so that its debit footing will show only those items called for in ¶159*a*, *b*, *c*. *Various methods for recording costs* of goods sold are employed. One is to enter both cost and selling price on orders, from which the cost price is tabulated for the period; another is to enter the cost price of each article sold in the sales book, or on sales ticket, their sum being the total cost of the goods sold for the period; the third is to make up a similar record from stock delivery orders. An entry for the month or period, debiting sales account and crediting finished goods account, is required. The sales account of a manufacturing concern is in every respect similar to the sales account of a trading business, described in ¶156 to ¶169 of this text. To eliminate an extra account, sales account may be debited for the cost of goods sold, instead of "cost of goods sold" account as stated. The difference between the two sides of the sales account would then show the gross trading profit for the period.

746. The various manufacturing accounts, as has already been stated under the several accounts, are connected with each other and with the factory cost accounts kept in subordinate ledgers and other account books of the factory, shop or works, which they control, through a series of entry books, variously designated as journals, or books, the name "journal," seeming to have the preference among accountants. These journals are as follows:

747. Invoice, or purchases journal. This book receives the entries for all materials purchased, whether raw or partly manufactured, which enter directly into the manufactured product, including freight and drayage and all other charges necessary to place the material in the stock-room ready for use. (¶705*a*) The entries are made from the invoices, and the freight, drayage, and other bills received. The total footing is debited to materials account and credited to accounts payable in the general ledger, the various items being debited in the materials, stock, or stores ledger, as described in ¶708. *When the voucher system* for recording purchase accounts is used, the debit to materials account is made from the vouchers payable register, which, of course, eliminates a separate purchases ledger which would otherwise be kept.

748. Transfer outward or requisition journal. All materials taken from stock on requisition, for work in process, are entered in this book from the requisition blanks, *at cost.* The total footing for the month is debited to materials in process account (¶711*a*) and credited to materials account (¶706*c*), while the items are credited to the proper accounts in the material, stock, or stores ledger. (¶708) When a single manufacturing account is kept (¶726), the total footing is debited to that account. (¶727*a*)

749. Transfer inward journal. In this book is recorded from "stock returned" cards, all entries for materials returned to the stock, or stores room, *at cost price,* which were previously credited to materials account. The total footing for the month is debited to the materials account in the general ledger (¶705*b*) and credited to materials in process account. (¶712*b*) The separate items are debited to the proper accounts in the materials, stock, or stores ledger, at cost price. (¶708)

750. Finished goods journal. When each order, job or contract is completed and the finished goods are ready for sale or have been placed in warehouse, an entry is made in this book from the factory cost cards, or job ledger, on which have been entered and totaled the separate costs of material, direct labor, and manufacturing expenses. This journal should, therefore, contain columns to receive these items. At the end of the month, the footing of the total column is posted to the debit of finished goods account (¶741*a*), while the footings of the credit columns are posted to the credit of materials in process account (¶712*c*), labor account (¶717*b*), and manufacturing, or factors expense account (¶722*c*) When a single manufacturing account, combining these credit accounts, is kept, they are credited to that account. (¶728*f*, *h*, *g*)

751. Stock deliveries journal. When this book is kept, it is necessary to enter only the numbers of the stock delivery orders or sales tickets, and the total cost of production price of each article, which may be taken from the original cost cards for the article or from the job ledger. The total for the month is posted to the debit of cost of sales account or to the debit of sales account, when that account is not kept. (¶745) It is credited to finished goods account. (¶742*b*)

752. Manufacturing expense estimate book. In this book is entered, at the beginning of each period, the estimated cost of each factory expense for the period covered in the estimate, which may be for the fiscal year or for a quarter or month. (¶720) The cost of these expenses is based largely upon the actual expenses of previous similar periods, with such changes as may be necessary. The total of these factory expenses equals the total manufacturing expense which is to be distributed over the work of the period then beginning, by one or the other of the

methods employed. (¶678, ¶679) It should be divided into monthly amounts which should be debited to manufacturing, or factors expense account (¶721*a*) and credited to factory expense account. (¶735*d*) If no entry is made of the estimated monthly manufacturing expenses, as suggested in ¶723*a*, ¶736, it should be carefully compared monthly with the balance shown by the manufacturing, or factors' expense account, as well as with the balance shown by the factory expense account. Varying conditions shown by idle productive factors caused by decreased production, labor troubles, overtime, and the various other elements affecting manufacturing costs, will usually require frequent changes to be made in the monthly estimate of manufacturing expenses (burden and overhead). This book, therefore, is of great importance in the efficient and economical administration of a manufacturing business.

Series of Entries Illustrating the Routine for Debiting and Crediting Accounts Under the Cost Method, From the Time Materials are Purchased Until the Finished Product is Sold.

753. Each step in the usual course of procedure in manufacturing is indicated in the following entries:

a. When materials are purchased to be used up in the manufacture of goods, the following accounts are debited and credited in the invoice, or purchases journal (¶747):

"Materials," Dr. (¶705*a*)	For cost of all materials, including transportation and other charges necessary to place the materials in the stock-room ready for use.
"Accounts Payable," Cr.	

b. When materials are taken from the stock-room on requisition, for use in the work-shop, the following accounts are debited and credited in the transfer outward journal (¶748):

"Materials in Process," Dr. (¶711*a*)	For the cost price of all materials received from the stock-room.
"Materials" Cr. (¶706*c*)	

c. When unused materials are returned to the stock-room, the following accounts are debited and credited in the transfer inward journal (¶749):

"Materials," Dr. (¶705*b*)	For unused material returned to the stockroom, at cost price.
"Materials in Process," Cr. (¶712*b*)	

d. When the daily, weekly or monthly pay-roll is made up, the accounts debited and credited from the pay-roll, time book or a list of the time cards, are as follows:

"Labor," Dr. (¶716*a*)		For direct labor.
"Factory Expense," Dr. (¶734*a*)		For indirect labor.
"Cash," Cr.	(or)	When paid in cash.
"Vouchers Payable," Cr.	(or)	When the voucher system is used and voucher is issued for pay-roll.
"Pay-Roll" Cr.		When such an account is kept for purpose described in ¶563.

Note—The proper account to be credited in connection with the pay-roll depends upon the system of accounts followed.

e. When orders, jobs or contracts are completed and the finished goods are ready for sale or have been placed in warehouse, and the burden and overhead expenses have been prorated and distributed on factory cost cards or job ledger, and the total cost of production, or "cost to make," has been determined, the following accounts are debited and credited in the finished goods journal (¶750):

"Finished Goods," Dr. (¶741*a*)
"Materials in Process," Cr. (¶712*c*)
"Labor," Cr. (¶717*b*)
"Manufacturing," or "Factors Expense" Cr. (¶722*c*)

For the cost of materials, direct labor, and of burden and overhead charges entering into the total cost of production.

f. When manufactured goods are sold, the following accounts are debited and credited:

"Accounts Receivable," Dr.
"Sales," Cr.

For the selling price of the goods sold.

g. When the cost of the goods sold is determined at the end of the month, the following accounts are debited and credited in the stock deliveries journal (¶751):

"Cost of Sales," Dr. (¶745)
"Finished Goods," Cr. (¶742*b*)

For the cost of the goods sold.

h. When a "cost of sales" account is not kept, sales account is debited in the foregoing transaction instead of "cost of sales" account. (¶745)

753*a* *In addition to the routine entries outlined in the preceding paragraphs,* there are a number of other entries which may be made necessary when there is a departure from the usual routine in the manufacturing processes; for instance, it is not unusual in manufacturing establishments, during dull seasons or when work is slack in any department, to partly manufacture or complete stock parts or materials ahead of the time when they are required for the completion of articles, by doing such machine or other work upon them as opportunity will permit. When this is done, an order is prepared, the materials are requisitioned, at cost price, from the stock-room, and the manufacturing process, whatever it may be, proceeds exactly as though they were to be at once completed, the productive labor and burden being charged as usual. When the work is carried as far as possible or until it is found necessary to discontinue it, the cost cards are made up for whatever work has been accomplished, and the new cost price determined, when the materials or parts are returned to the stock-room. When this is done, the entry shown in ¶ 753*e* would be made, at the new cost price, except that materials account would be debited instead of finished goods account, and the entry, of course, would be made in the general journal instead of in the finished goods journal.

(*b*) Another instance is where finished parts or materials in the stock-room are sold as in the case of automobile or other machine parts. While the article would be credited to sales account at selling price, it must be credited to materials account at cost price, which would require a general journal entry, debiting cost of goods sold account and crediting materials account to adjust.

(*c*) A third illustration is where finished parts or articles that have been charged to finished goods account and placed in the sales-room or warehouse, are returned to the work-shop to be used for the completion of some other article; for instance, where finished valves, oil cups or the like are used in the completion of an engine in process of building. In such cases, materials in process should be debited and finished goods credited, at the total factory cost of the article, through the general journal or through a special journal kept for that purpose. Other transfers of materials or products in various stages of manufacture, outside of the usual routine, may require corresponding entries, which may be easily determined by a consideration of the accounts involved.

754. Inventories of manufacturing accounts. Separate inventories are required of materials, (¶706*e*) materials, in process, (¶712*c*) labor, (¶717*c*) manufacturing expenses, (¶722*e*) factory expenses, (¶735*f*) and finished goods, (¶742*c*) prior to the preparation of the manufacturing statement. These inventories are invariably taken at cost price.

a. The materials inventory consists of a list of the materials on hand in the stock, or stores room, taken at cost price, which must agree with the accounts in the stock, or stores ledger or on cards. Where purchases of the same article are made at different prices, the *average* price must be ascertained or separate accounts for different prices may be opened.

b. The materials in process inventory is made up from the cost cards or from the job ledger for each of the orders, jobs or contracts which are uncompleted. Where the materials were purchased at different times at different prices, the *average* price for the materials in each order, job or contract must be ascertained, or separate accounts may be kept with the same items at different prices.

c. The labor inventory consists of the direct labor on uncompleted orders, jobs or contracts, made up from the cost cards or job ledger.

d. The manufacturing expense inventory consists of all manufacturing expenses yet to be charged to work in process. When manufacturing expenses are distributed on a percentage basis, this inventory is found by calculating the manufacturing expenses that have accrued on the uncompleted work in process. (Read ¶723; then read ¶724). If manufacturing expenses are distributed through machine, productive factor or productive center time, the inventory would include any productive hours that have not been charged on the cost cards or in the job ledger, and any idle machine hours if idle time has not been included in the supplementary rate. A separate record should be kept of idle machine hours, which, taken in connection with the results shown by the manufacturing account, would give a complete analysis of manufacturing expenses and shop, or works, efficiency.

e. Factory expense inventory is similar to the ordinary expense inventory. (¶464–474*c*) These inventories, like the other manufacturing account inventories should be treated as directed in rule 172.

f. Finished goods inventory is in every way similar to merchandise inventory, described in ¶169, except that it is always taken at cost price, whereas, if there has been any depreciation or change in value, it should be disposed of as instructed in ¶169*a*.

MANUFACTURING STATEMENTS.

755. Four principal statements are usually prepared at the close of each fiscal period from the books of a manufacturing business: the manufacturing statement, to show the cost of production of goods manufactured during the year or other fiscal period; the trading statement, to show the gross trading profit or the gross trading loss from sales for the period (¶234); the profit and loss statement, to show the net profit or the net loss for the period and its disposition at the close of the period (¶437); and the statement of resources and liabilities, or balance sheet, for the period (¶487). The first of these statements is peculiar to the manufacturing business; the last three are in every way similar to those of a trading business, which are fully explained in previous chapters.

756. The form of the manufacturing statement is determined, to some extent, by the classification of the accounts in the general ledger, which is also true of the results shown in the final trial balance from which the statement is prepared. When the department method of accounts is followed, the final trial balance supplies most of the data for a very comprehensive proof statement showing the disposition of the various cost elements in the manufacturing processes. When the cost method of accounts is followed, the trial balance and the accompanying statement are usually much briefer, as the various cost elements are fully accounted for, proven and disposed of in the current control accounts, although the manufacturing statement may be made as complete as desired by going to the ledger accounts for supplementary information.

756*a*. *The difference in results shown* in the trial balances of two groups of manufacturing accounts, both made up from the same series of transactions, one group kept by the department method and the other group by the cost method, is strikingly illustrated in the trial balances shown in illustrations 103 and 108, and the manufacturing statements made up from each. These differences are noted in the explanations showing the reconciliation between them.

757. To show cost elements and their disposition in detail, manufacturing statements should be prepared in two parts, the first part to show the *prime cost* of the goods manufactured or partly manufactured for the period, the second part to show the *factory cost*, or *cost of production*, of the goods manufactured for the period, corresponding with the first two items in the cost formula, ¶664. Part 1 is made up from those accounts which show cost of materials and of direct labor, and of any other items that enter into the *prime cost* of the goods manufactured or partly manufactured. Part 2 is made up from those accounts which show the cost of the manufacturing expenses (burden and overhead), and of any other items which, added to prime cost, enter into the *total cost of production* of the goods manufactured.

FORMULA FOR MANUFACTURING STATEMENT

PART 1, showing *prime cost.*

758. Elements of cost for period consist of:

a. Cost of materials on hand at the beginning of period, as shown by inventory or by balance of materials account. (¶ 707)

b. Cost of partly manufactured goods on hand at the beginning of period, including cost of materials and direct labor (prime cost), as shown by inventories; or, when the cost method of accounts is followed, by balances of "materials in process" and "productive labor" accounts for the previous period. (¶ 713, 718)

c. Cost of purchases for the period, less returns and allowances, as shown by the material accounts when kept under either the department or cost method. (¶705*a*)

d. Cost of productive labor (direct labor) for the period, as shown by the labor account. (¶ 716*a*)

759. Disposition of costs shown in:

e. Cost of goods manufactured during period, including cost of material and direct labor (prime cost), as shown by the material and labor accounts; or, when the cost method of accounts is followed, as shown by credits to the "materials in process" (¶ 712*c*) and "productive labor" (¶ 717*b*) accounts, the contra of which is charged to finished goods account.

f. Cost of partly manufactured goods on hand at the close of the period, valued at prime cost, as shown by unfinished orders, jobs or contracts; or, when the cost method of accounts is followed, by the sum of the balances of "materials in process" (¶ 713) and "productive labor" accounts (prime cost). (¶ 718)

g. Cost of materials on hand at the close of the period, shown by the inventory; or, when the cost method of accounts is followed, by the balance of the materials account. (¶ 707)

PART 2, showing *cost of production.*

760. Elements of cost consist of:

h. Cost of manufacturing expenses at beginning of period, as shown by inventory; or, when the cost method of accounts is followed, by the balance of manufacturing expense account at the beginning of period. (¶723)

i. Cost of goods manufactured during the period, as described in item "e" above (prime cost).

j. Cost of manufacturing expenses for the period, as shown by the manufacturing expense account or accounts for the period. (¶ 721*a*, *b*)

761. Disposition of costs shown in:

k. Cost of manufacturing expenses on partly manufactured goods, at the close of the period, as shown by the balance of manufacturing expense account or accounts. (¶ 723)

l. Cost of goods manufactured during the period, at *total cost of production,* as shown by finished cost sheets or orders; or, when the cost method of accounts is followed, by the amount charged to finished goods account for the period. (¶ 741*a*)

762. The elements of cost included in a complete manufacturing statement for a given period may be clearly understood from the *formula* opposite, in which the items are shown in the position and order in which they should appear in the statement. It will be observed that a statement prepared after this formula will show not only the various elements of cost entering into the total cost of production, but also a proof of the correct distribution of these costs by accounting for them in the completed and partly manufactured goods for the period, and in the proven balances shown by the control accounts.

763. A final trial balance, taken from a set of books in which the manufacturing accounts are kept by the department method (¶687), is shown in illustration 103. The manufacturing accounts are indicated by the letter "M" in the margin.

ILLUSTRATION 103

TRIAL BALANCE, DECEMBER 31, 19 . TODD MFG. CO.

	Cash - per C. B.	10200	00		
	Cash - petty	200	00		
M	Materials and supplies	3800	00		
M	Material in process	2700	00		
M	Labor in process — Inventories, Jan. 1, 19	1400	00		
M	Manufacturing expenses	850	00		
	Finished goods	7000	00		
	Accounts Receivable	17500	00		
	Machinery	29000	00		
	Small Tools	1800	00		
	Office furniture and fixtures	500	00		
	Store Fixtures	500	00		
	Accrued Taxes			100	00
	Accrued Pay-roll			1200	00
	Accounts Payable			6000	00
	Surplus			8200	00
	Reserve for Uncollectable Accounts			350	00
	Reserve for Depreciation on Machinery, etc.			1500	00
	Capital Stock - Preferred 250 shares at $100			25000	00
	Capital Stock - Common 250 " "			25000	00
M	Materials Purchased	53000	00		
M	Labor	34000	00		
	Sales, less returns, allowances & discounts			116200	00
M	Manufacturing Expenses	12000	00		
	Selling Expenses	5000	00		
	Administrative Expenses	4100	00		
		183550	00	183550	00

764. Inventories. The inventories at the close of the period, December 31, are as follows: materials and supplies, $8500; materials in process, $4200; labor in process, $1750; manufacturing expenses, $1480; finished goods, $9420.

ILLUSTRATION 104

MANUFACTURING STATEMENT FOR YEAR ENDING DECEMBER 31, 19 .

Part 1. Prime Cost.

759a	INVENTORIES, Jan. 1, 19 ,		
	Materials and supplies at cost		3800
759b	Materials in process - partly mfg'd goods	2700	
	Labor in process - "	1400	4100
759c	PURCHASES OF MATERIALS and other manufacturing supplies during period, including inward freight and expressage, less returns, allowances, discounts, etc.		53000
759d	PRODUCTIVE LABOR for period		34000
			94900
	Production Cost.		
761b	MANUFACTURING EXPENSES of preceding period applicable to partly manufactured goods		850
761e	PRIME COST of goods manufactured during period, brought down		80450
761f	MANUFACTURING EXPENSES during period: -		
	Rent of factory	2200	
	Taxes of factory	200	
	Stationery and supplies	100	
	Insurance on materials and machinery	500	
	Superintendence	1500	
	Wages of foreman and factory clerks	2400	
	Wages of firemen, engineers and oilers	2500	
	Fuel and lighting	500	
	Repairs and renewals on machinery	600	
	Depreciation on machinery	1500	12000
			93300

765. Manufacturing statement—department method of accounts. The statement in illustration 104 is made up from the trial balance, illustration 103, and the inventories at the close of the period. The American, or standard form of statement is shown in the illustration. The items in detail, entering into the total manufacturing expenses as shown on the statement, were found by an analysis of the manufacturing expense account. The same is true of the items making up the total selling expenses and the total administrative expenses shown in illustrations 105 and 106.

766. Preparation of the manufacturing statement when manufacturing accounts are kept by the department method. Explanation: Notice that Part 1 of the statement shows *prime cost*, and that Part 2 shows *cost of production*, in agreement with the formula for manufacturing statement. (¶664)

Part 1.

(1) *Inventories, January 1, 19* , consisting of three items, are inventories at the close *of the last preceding fiscal period*, taken from the trial balance. (¶ 174)

(2) *Purchases of materials* are shown by the debit balance of materials account in the trial balance.

(3) *Productive labor* is shown by the debit balance of the labor account in the trial balance.

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760d	PRIME COST (materials and labor) of goods manufactured during period, carried down			80450
760g	INVENTORIES, Dec. 31, 19 ,			
	Materials and supplies, at cost			8500
	Materials in process - partly mfg'd goods		4200	
760f	Labor in process - "		1750	5950
				94900
762d	MANUFACTURING EXPENSES applicable to partly manufactured goods			1480
762f	PRODUCTION COST of goods manufactured during period, carried to trading statement			91820
				93300

(4) *Prime cost* is the difference between the debit items showing cost of material and productive labor, and the credit items showing the inventories at the close of the period, *i.e.*, it represents the cost of the material and labor entering into the goods manufactured during the period.

(5) *Inventories, December 31, 19* , consisting of three items, are the inventories at the close *of the present fiscal period.* (¶174) After this item is entered, Part 1 of the statement should be footed and ruled, as shown in the illustration.

Part 2.

(6) *Manufacturing expenses* during preceding period, the first item on the debit side of Part 2, is the inventory of manufacturing expense account at the close of the last preceding fiscal period, as shown in the trial balance.

(7) *Prime cost* is the first item on the credit side of Part 1 brought down.

(8) *Manufacturing expenses* for the period are found in the debit balance of manufacturing expense account in the trial balance, the various items being found by an analysis of that account.

(9) *Manufacturing expenses,* the first item on the credit side, is the amount of the inventory of these expenses at the close of the present fiscal period.

(10) *The production cost* of the goods manufactured during the period is the difference between the sum of the debit and the credit items, which completes Part 2 of the statement. The production cost, represented in the last credit item, is the connecting link between the manufacturing and the trading statement, that item being shown as the second item on the debit side of the trading statement.

ILLUSTRATION 105

TRADING STATEMENT FOR YEAR ENDING DECEMBER 31, 19 .

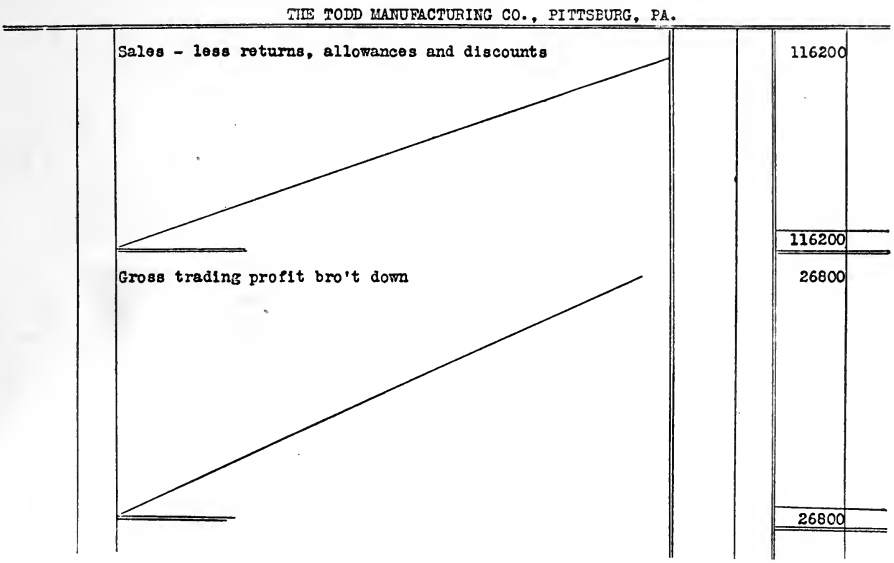
INVENTORY, Dec. 31, 19 ,		
Manufactured goods on hand at close of preceding period		7000
GOODS MANUFACTURED during period, per manufacturing statement		91820
Total cost of manufactured product		98820
Less INVENTORY manufactured goods on hand, at close of this period, Dec. 31, 19 ,		9420
Cost of goods sold		89400
Gross trading profit carried down		26800
		116200
SELLING AND DISTRIBUTING EXPENSES		
Freight outward	100	
Commission for selling	200	
Salesmen's salaries	2500	
Wages of shippers and packers	600	
Insurance on stock, etc.	50	
Traveling expenses	1230	
Supplies	50	
Advertising	100	
Heat and light	10	
Rent show-room	100	
Storage, - outside warehouse	50	
Depreciation on fixtures	10	5000
NET TRADING PROFIT carried to profit and loss statement		21800
		26800

767. Trading statement. This statement is similar in all essential particulars to the trading statement of a mercantile business. (¶240) It is shown in illustration 105. The statement of resources and liabilities is shown in illustration 107.

ILLUSTRATION 106

PROFIT AND LOSS STATEMENT FOR YEAR ENDING DECEMBER 31, 19 .

ADMINISTRATIVE EXPENSES		
Rent of offices	100	
Insurance on furniture & fixtures	16	
Taxes - proportion	50	
Interest on loans	30	
Officers' salaries	2000	
Clerks' salaries	1000	
Audit fee	200	
Stationery and office supplies	50	
Heat and light	100	
Repairs, office furniture	60	
Reserve for doubtful accounts	400	
Depreciation on furniture	92	4100
NET PROFIT for period, carried down		17700
		21800
DIVIDEND Preferred stock, $25000, at 7%	1750	
Common stock, $25000, at 10%	2500	4250
SURPLUS PROFITS carried down		13450
		17750
Surplus, Dec. 31, 19 , as shown on balance sheet		21650
		21650



768. Profit and loss statement. This statement, shown in illustration 106, while similar to the profit and loss statement explained in ¶435–445 is divided into three parts, the first showing the net profit for the period, the second showing the distribution of the net profits for the period, and the third showing the undivided profits, or surplus, of the business at the close of the period.

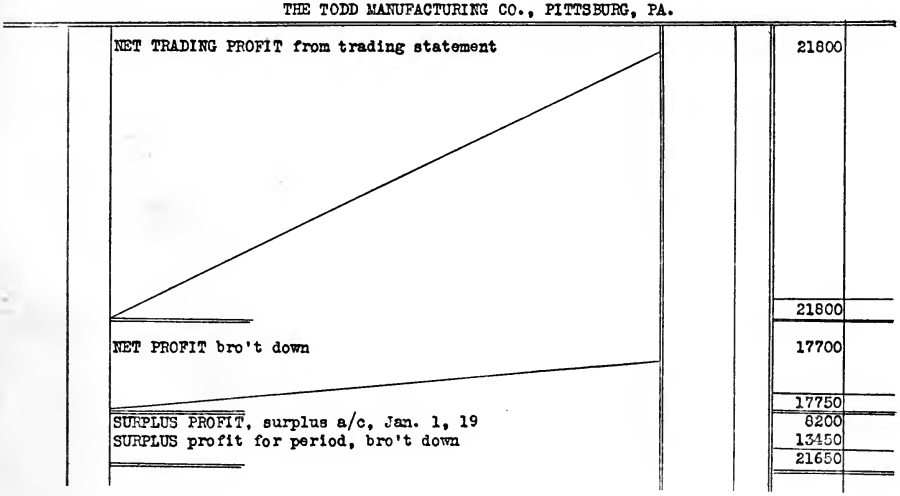


ILLUSTRATION 107

STATEMENT OF RESOURCES AND LIABILITIES, DECEMBER 31, 19 .

Cash in office	200	
Cash in bank	10200	10400
Inventories, -		
Materials in stock	8500	
Materials in process	4200	
Labor on materials in process	1750	
Manufacturing expenses	1480	
Finished goods in stock	9420	25350
Accounts receivable	17500	
Less reserve for uncollectable accounts	350	17150
Total current resources (assets)		52900
Machinery	29000	
Less reserve for depreciation	1500	27500
Small tools		1800
Office furniture and fixtures	500	
Store fixtures	500	1000
Total resources		83200

ILLUSTRATION 108

FINAL TRIAL BALANCE, DECEMBER 31, 19 . THE TODD MFG. CO.

Cash - per C. B.	10200	
Cash - petty	200	
Materials	8500	
Materials in Process	4200	
Productive Labor	1750	
Manufacturing Expense	1480	
Finished Goods	9420	
Accounts Receivable	17500	
Machinery	29000	
Small Tools	1800	
Office Furniture & Fixtures	500	
Store Fixtures	500	
Accrued Taxes		100
Accrued Pay-roll		1200
Accounts Payable		6000
Surplus		8200
Reserve for Uncollectable Accounts (contra in admr. ex. a/c)		350
Reserve for Depreciation on Machinery, etc. (contra in Mfg. Exp. & Factory Exp.)		1500
Capital Stock Preferred - 250 shares at $100		25000
Capital Stock Common - 250 " " 100		25000
Cost of Sales	89400	
Sales		116200
Selling Expense	5000	
Administrative Expense	4100	
	183550	183550

769. **The final trial balance, taken from a set of books in which the manufacturing accounts are kept by the cost method** (¶689), is shown in illustration 108. The amounts were made up from exactly the same transactions that entered into the accounts shown in the trial balance in illustration 103. It will be noted that the trial balance under the cost method is considerably shorter, and that the balances shown by the manufacturing accounts differ from those

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Accrued taxes, - estimated		100
Accrued labor		1200
Accounts payable		6000
Total current liabilities		7300
Dividends declared		
Preferred stock, $25000, at 7%	1750	
Common " 25000, " 10%	2500	4250
Total liabilities		11550
Capital stock issued		
Preferred	25000	
Common	25000	50000
General Profit and Loss account		
Surplus, Jan. 1, 19 ,	8200	
" Dec. 31, 19 ,	13450	21650
		83200

shown in the trial balance under the department method. When both methods are thoroughly understood, however, it is not difficult to reconcile the manufacturing accounts of one trial balance with those of the other, as is explained in ¶771. It should also be noted that while the balances of the materials, materials in process, productive labor, manufacturing expense, and finished goods accounts in illustration 108 show the inventory value of those accounts *at the close of the present fiscal period,* the balances shown by similar accounts in illustration 103, under the department method of accounts, show the inventory values *at the close of the last preceding fiscal period.*

770. An interesting exhibit of the manufacturing accounts under the cost method may be had by opening each account with the inventories shown in the trial balance, illustration 103, and posting the journal entries, shown in illustration 109, which represent in totals the entries made during the year in the various cost journals. It will be seen that the balances shown by these accounts at the close of the period agree with the balances shown in trial balance, illustration 108.

ANALYSIS SHOWING AGREEMENT OF MANUFACTURING ACCOUNTS IN TRIAL BALANCE, ILLUSTRATION 108, WITH SIMILAR ACCOUNTS IN TRIAL BALANCE, ILLUSTRATION 103.

771. This analysis explains the essential differences between the cost and the department methods of accounts. It shows also that while the results are different in each corresponding account, they are, in fact, harmonious, each being correct under the method employed for keeping it.

ILLUSTRATION 109

SERIES OF ENTRIES SHOWING AGGREGATE AMOUNTS DEBITED AND CREDITED TO MANUFACTURING ACCOUNTS FOR THE YEAR, PER THE COST METHOD.

Par.				
747	Materials	Purchases	53000	
	Accounts Payable			53000
748	Materials in Process	Requisitions	50600	
	Materials			50600
749	Materials	Returned to stores	2300	
	Materials in Process			2300
	Productive Labor	Pay-roll from cash book	34000	
	Cash			34000
	Manufacturing Expenses	Estimate for year, per	12000	
	Factory Expenses	general journal		12000
750	Finished Goods		91820	
	Materials in Process			46800
	Productive Labor			33650
	Manufacturing Expense			11370
751	Cost of Sales	General journal	89400	
	Finished Goods			89400

ILLUSTRATION 110

Materials

Jan 19	1	Bal. brot down		3800	Dec 19	31	Requisitions for yr	50600	
Dec	31	Pchs for year		53000		31	Balance - Inventory	8500	
	31	Rtd materials		2300	Red				
				59100				59100	
Jan 19	1	Bal. brot down		8500					

(*a*) *Materials account.* This account, illustration 110, is debited, first, with the balance brought down from the last preceding fiscal period, December 31, $3800. This amount corresponds with the amount shown as the inventory of materials and supplies in trial balance, illustration 103. The materials account is then charged with the materials purchased for the period, $53000 (¶705*a*), and with the materials returned from work in process, $2300. (¶705*b*) It is credited with the amount of material requisitioned for work in process during the period, $50600 (¶706*c*), the balance of the account, $8500, being the amount shown on trial balance, illustration 108. (¶707)

ILLUSTRATION 111

Materials In Process

19 Jan	1	Bal. brot down		2700	19 Dec	31	Mtls returned		2300
Dec	31	Requisitions for yr		50600		31	Finished goods		46800
					Red	31	Balance-Inventory		4200
				53300					53300
19 Jan	1	Bal brot down		4200					

(*b*) *Materials in process account.* The balance in this account, $2700, illustration 111, agrees with the item for that account in trial balance, illustration 103. It is then charged with all goods requisitioned from the materials account for the period. (¶711*a*) The account is credited for any materials returned to the store-room and charged back to the materials account (712*b*), and for the amount of material used in finished orders, jobs or contracts, at cost. (712*c*) The balance of the account shows the cost of the material in the uncompleted work in process, $4200, being the amount shown on trial balance, illustration 108. (¶713)

ILLUSTRATION 112

Productive Labor

19 Jan	1	Bal. brot down		1400	19 Dec	31	Finished goods		33650
Dec	31	Pay-roll for yr		34000		31	Balance-Inventory		1750
					Red				
19 Jan	1	Bal. brot down		1750					

(*c*) *Productive labor.* The balance brought down in this account is $1400, agreeing with the inventory of labor in process in trial balance, illustration 103. The account is then charged with direct labor for the period (¶716*a*), and is credited with the direct labor expended in goods manufactured for the period (¶717*b*), the balance of the account, $1750, agreeing with trial balance, illustration 108. (¶718)

ILLUSTRATION 113

Manufacturing Expenses

19 Jan	1	Bal. brot down		850	19 Dec	31	Finished goods		11370
Dec	31	Charged for yr		12000	Red	31	Balance-Inventory		1480
				12850					12850
19 Jan	1	Bal. brot down		1480					

(*d*) *Manufacturing expense.* On trial balance, illustration 103, $850 is shown as the amount of the inventory for this account, brought down from the previous period, which agrees with illustration 113. It is then charged with the estimated manufacturing expenses, $12000. (¶721*a*, *b*) It is credited for the expenses distributed in the goods manufactured (¶722*c*), the balance, $1480, agreeing with the item in trial balance, illustration 108. (¶723)

ILLUSTRATION 114

Finished Goods

19					19			
Jan	1	Bal. brot down	7000		Dec	31	Cost of sales per P	89400
Dec	31	Mfd during year	91820			31	Balance-Inventory	9420
			98820					98820
19								
Jan	1	Bal. brot down	9420					

(*e*) *Finished goods account* shows a balance brought down of $7000, corresponding with the inventory in trial balance, illustration 103. It is charged with $91820, the cost of the goods manufactured during the period. (¶741*a*) It is credited for the cost of the goods sold during the period, $89400 (¶742*b*), the balance of the account, $9420, agreeing with trial balance, illustration 108. (¶743)

772. **A careful study of these ledger accounts** and the references given, will show that all the elements of cost included in the manufacturing statement, made up from the manufacturing accounts kept by the department method, illustration 103, have been included, proven and disposed of in the manufacturing accounts kept by the cost method, the final results being shown in the balances of the accounts and in the debit of $91820 to finished goods account, the connecting item between the group of manufacturing accounts and the group of selling accounts being the cost of the goods sold, $89400, which is the total credit to finished goods account for the period.

773. **Manufacturing statement—cost method of accounts.** When the manufacturing accounts are kept by the cost method, the manufacturing statement shown in illustration 104 may be prepared, but the accounts in the ledger must be referred to for part of the information necessary, as follows:

Part 1.

(1) *Inventories, January 1, 19* , instead of being taken from the trial balance, illustration 103, are found in the inventory balances of the materials, materials in process, and productive labor accounts, brought down from the preceding fiscal period, January 1, as shown in the accounts in illustrations 110–114.

(2) *Purchases of materials,* $53000, is the sum of the purchases for the period shown on the debit side of the materials account, exclusive of the items for materials returned from work in process and the balance of the account at the beginning of the period. See illustration 110.

(3) *Productive labor.* $34000, is shown by the debit footing of productive labor account, exclusive of the inventory at the beginning of the period.

(4) *Prime cost of goods manufactured,* $80450, is the sum of the credit footing of materials in process account less items of materials returned to stockroom, $46800, and the credit footing of productive labor account, $33650.

(5) *Inventories, December 31, 19* , are shown by the balances of the materials, materials in process, and productive labor accounts, as shown in the trial balance, illustration 108. These balances equal the inventory value, at cost price of the materials in stock, materials in process of manufacture, and productive labor charged to work in process. (¶ 707, 713, 718)

This completes Part 1 of the manufacturing statement, under the cost method, and the footings of the two sides of the statement must be equal, *i.e.*, all of the costs charged on the debit side of the statement are accounted for on the credit side of the statement, the balances being supported by inventories, which are again proven by the various subordinate factory books and journals, such as the materials ledger, etc.

Part 2

(6) *Manufacturing expenses* during preceding period, the first item on the debit side of Part 2, is the balance of the manufacturing expense account brought down from the preceding fiscal period, as shown in that account in illustration 113.

(7) *Prime cost* of goods manufactured during the period is the amount shown in item 1 on the credit side of Part 1 of the statement, brought down. (See ¶ 773 (5)).

(8) *Manufacturing expenses* for the period are shown by the debit footing of manufacturing expense account, exclusive of the inventory of the preceding period, brought down January 1.

(9) *Manufacturing expenses,* the first item on the credit side of Part 2, is the inventory value of these expenses at the close of the present fiscal period, shown by the balance of manufacturing expense account. (¶ 723)

(10) *The production cost* of goods manufactured during the period $91820 is the debit footing of finished goods account, exclusive of the balance of the account for the preceding fiscal period, brought down January 1. It is the amount charged to finished goods account during the period from the finished goods journal and equals the sum of the credits to materials in process ($46800), productive labor ($33650), and manufacturing expenses ($11370). (¶712*c*, 717*b*, 722*c*)

774. Manufacturing accounts, under the cost method, are self-proving. On the debit side they show the costs of material, labor and manufacturing expenses; on the credit side they show the disposition of these costs through the various manufacturing processes until the final result, shown in the total cost of production, is reached, for which finished goods account is debited. (¶741*a*) The balance shown by each account is also self-proving, as it must agree with the inventories and the results shown by the various supplementary cost books and records, such as the materials and stock ledgers, cost cards, sheets, and summaries. For this reason, the manufacturing statement is frequently omitted, the "cost of merchandise sold" being the connecting item between the manufacturing and the trading accounts, as shown in illustration 114. It will be noticed that the trading and profit and loss statement, illustration 115, is in report form. It may be prepared in the standard form, as shown in illustrations 105, 106.

ILLUSTRATION 115

TRADING AND PROFIT & LOSS STATEMENT, DECEMBER 31, 19

Gross Sales	116500	
Less returns, allowances & discounts	300	
Net Sales		116200
Less cost of merchandise sold		89400
Gross trading profit for period		26800
Less Selling expenses, viz.,		
Freight outward	100	
Commissions	200	
Salesmen's salaries	2500	
Wages shippers and packers	600	
Insurance on stock	50	
Traveling expenses	1230	
Supplies	50	
Advertising	100	
Gas, fuel and light	10	
Rent	100	
Storage (outside warehouse)	50	
Depreciation on Fixtures	10	5000
Net Trading profit for period		21800
Administrative expenses, -		
Rent (proportion)	100	
Insurance on fixtures	18	
Taxes (proportion)	50	
Int. on temp. loan	30	
Officers' salaries	2000	
Salaries of office clerks	1000	
Audit fee	200	
Stationery & office supplies	50	
Gas, fuel and lighting (proportion)	100	
Repairs - office fixtures	60	
Uncollectable accounts (Charge for contra to reserve)	400	
Depreciation on fixtures	92	4100
Net profit for period		17700
Dividend declared, -		
Preferred stock, $25000, at 7%	1750	
Common " 25000, " 10%	2500	4250
Balance to Surplus a/c		13450

775. A statement of manufacturing operations may be prepared to accompany the preceding trading and profit and loss statement, if desired. By referring to the ledger accounts, illustrations 110–114, it will be seen that this statement is nothing more than a statement in report form of the facts shown by those accounts.

ILLUSTRATION 116

STATEMENT OF MANUFACTURING OPERATIONS FOR YEAR ENDING DECEMBER 31, 19 .

THE TODD MFG. CO., PITTSBURG, PA.

MATERIALS A/C		
Inventory and supplies, Jan. 1, 19 ,	3800	
Purchases during period	53000	56800
Materials requisitioned for work in process	50600	
Less materials returned to stock	2300	
Cost of materials transferred to work in process, during period		48300
Balance a/c - Materials on hand, per inventory		8500
MATERIALS IN PROCESS A/C		
Inventory materials in process partly manufactured, Jan. 1, 19 ,	2700	
Materials requisitioned during period, less returns	48300	51000
Less Cost of materials in the completed product of the period		46800
Balance a/c - Materials in process at close of the period		4200
PRODUCTIVE LABOR A/C		
Inventory of labor on materials in process, partly manufactured Jan. 1, 19 ,	1400	
Labor on completed and partly manufactured goods for the period	34000	35400
Less Labor expended on completed goods		33650
Balance a/c - Labor on uncompleted work in process, at close of period		1750
MANUFACTURING EXPENSE A/C		
Inventory of expenses on goods in process, partly manufactured Jan. 1, 19 ,	850	
Manufacturing expenses for period	12000	12850
Less Mfg. expenses charged to completed goods		11370
Balance a/c - Expenses on uncompleted work in process, at close of period		1480
FINISHED GOODS A/C		
Inventory, Jan. 1, 19 ,	7000	
Cost of goods manufactured during period		
Materials 46800		
Labor 33650		
Mfg. Expenses 11370		
	91820	98820
Less - Cost of goods sold during the period, carried to trading statement		89400
Balance - Inventory on hand Dec. 31, 19 ,		9420

Forms of Cost Records, Reports, Books, Accounts, Statements, Etc.

776. These forms may be designed in great variety, and for many purposes. Those shown in the following illustrations are general in character, and are intended to offer suggestions for forms that could be used for the purposes named, rather than to be considered as exact models, since they would likely have to be changed considerably, in size and descriptive matter, to meet the requirements of a particular cost system. The various journals receiving entries from these forms are frequently ruled to correspond. Such of the forms as can be conveniently printed and made out in copying ink, may be copied in the appropriate journals made up of copy paper, from which abstracts, or recapitulations, may be made up at the close of each month.

Illustration 117

ORDER

Date_____ 19__. No.____

Make for _____ Address _____

Date Wanted _____ Date Completed _____

Here follows description of article, with instructions, drawings, etc.

Material Req. No. _____ Routed by _____

Put in process _____ Shop order No. _____

Illustration 117. This is a suggestion for the form of an order, issued by the office to the superintendent of the factory or works for the making of a certain article or goods. It is usually accompanied by a requisition for the materials, and not infrequently by drawings, blueprints, detailed instructions and, where works are thoroughly organized, by a routine, or process sheet, indicating exactly, in detail, the various processes to be followed and the productive factors to be employed, from the time the order is received in the works until the finished goods are completed.

Illustration 118. This is a suggestion for a requisition blank, which is made out in the office, usually in triplicate, one copy going to the store, or stock-keeper, another following the goods to the work-shop, the third being retained in the office, where it is entered in the requisition journal. (¶. 748)

ILLUSTRATION 118

REQUISITION FORM.

Req. No. _____ Date _____

Storekeeper - Delivery account of

Order Number	Stock Number	Quantity	Particulars	Cost	Amount

Delivered by _____ Signed _____
Received above _____
Ent'd Mat. Stock Ledg., page _____
Order charged, Cost Rec. _____
Ent'd Req. Journal, page _____

ILLUSTRATION 119

MATERIALS RETURNED.

Return No. _____ Date _____

Storekeeper - Credit returned material account of

Order Number	Stock Number	Quantity	Particulars	Cost	Amount

Storekeeper receipt _____ Signed _____
Returned by _____
Ent. Raw Mat. Stock Ledg., page _____
Order credited, Cost Rec. _____
Ent. Trans. In. Jour., page _____

Illustration 119. This is a suggestion for a blank which is made out when materials are returned from the work-shop to the stock-room. It is entered in the transfer inward journal. (¶. 749) The items and the amounts in this, as well as in the requisition form, shown above, are entered in the stock ledger.

Illustration 120 shows the form of a stock card, where the card system is used, or the rulings of a materials ledger. Not infrequently the ordinary form of ledger is used. Many prefer the loose-leaf form of ledger for this purpose.

ILLUSTRATION 120

STOCK CARD

Raw Material

Classification No. _____

Maximum _____

Minimum _____

Location _____

Article _____

Received					Delivered					Balance			
Date	Sheet No.	Quantity	Price	Amount	Date	Sheet No.	Quantity	Price	Amount	Date	Quantity	Price	Amount

ILLUSTRATION 121

DAILY TIME TICKET

_____ Department Date _____

Name _____ Clock No. _____

Occupation _____ Room _____

Order No.	Kind	Operation	Quantity	Time	Rate	Amount
Quantity O. K.		Price O. K.			Amount O. K.	

ILLUSTRATION 122

MACHINE TIME TICKET

Machine No. _____ Operator _____

Article _____

Time begun _____ Finished _____

Total time _____ H'rly rate _____ Amt. $ _____

Chg'd by _____ Cost sheet No. _____

Detail

Date	Operation	Remarks	No. hrs.

Illustrations 121 and 122. These are simple forms, which explain themselves. The daily time ticket shows the time of the workman for the day. It may be made in the form of a weekly time statement. The machine time ticket is used to record the daily work performed by each machine, and should check against the order or job cards following each article through the factory. The pay-roll is made up from the daily time tickets.

ILLUSTRATION 123

COST SHEET

Cost of _____

For _____ Address _____

Order No. _____ Date Issued _____ Completed _____ Billed _____

Materials				Productive Labor					Manufacturing Expenses				
Date	Req. No.	Quantity	Amount	Date	Ticket No.	No. hr's	Rate	Amount	Date	Factor No.	Time	Rate	Amount

SUMMARY

	Cost	Estimated	Increase	Decrease	How Accounted For	
Materials Productive Labor Mfg. Expenses Total Fac. Cost Selling Exp. Profit Selling Price						Correct _____ Cost Clk. Examined _____ Supt. Approved _____ Mgr.

Illustration 123. Cost sheets are usually kept in the office, but a cost card, ruled like the form of the cost sheet shown above the summary, usually follows each order, job or contract through the factory. This job card, as it is usually called, is sent to the office daily, and it is from this card that the cost sheet is made up. When bound they are called job ledgers. When the work is completed, the summary is filled out and proper entries are made in the finished goods journal (¶ 750), which completes the record of the manufacturing process. The illustration shows only one of many different forms of cost sheets and of job cards, which vary according to the requirements of the shop in which they are used. Frequently they are bound in loose leaf ledger form.

It should be noted that in all the illustrations of forms, no attempt has been made to show the proper width of columns or maintain uniformity in the spaces, that being determined in the forms by the size of the headings.

THE VOUCHER SYSTEM

777. This is a name given to a method of recording purchase transactions, whereby a separate account with each person from whom a purchase is made becomes unnecessary, the aggregate total of such accounts being carried in an accounts payable, or vouchers payable, account, which in every particular corresponds with the accounts payable account described in ¶50, illustration 9.

ILLUSTRATION 124

VOUCHER

Date	Vo. No.	Name	Address	Materials Dr.	Productive Labor Dr.	Selling Expense	
						Advertising Dr.	Other Expense Dr.

778. The advantages of the voucher system are so many that it has been adapted to meet the requirements of all lines of business. It is particularly useful in distributing costs in department accounts, cost accounts, supplementary expense accounts, and, in fact, all classes of accounts where considerable detail is desired. It may be used with almost equal facility whether a cash or credit business is conducted.

779. A voucher, in the ordinary business sense, is a name that is applied to any approved paper or document which is accepted as a truthful exhibit of business transactions, such as receipts, paid notes, acceptances and checks, certified bills, invoices, etc. A voucher is also termed a "warranty of title." *As applied to the voucher system of accounts,* it refers to a printed form attached to or relating to bills purchased, which contains a statement certifying to the correctness of the bills and the purpose for which the amount called for in the voucher is contracted.

ILLUSTRATION 125

Pittsburg, Pa., _____ 19___

Todd Manufacturing Co.,

To _____

Date	Description	Amount

Approved _____ Pres. Examined _____ Mgr.

REGISTER

Administration Expense Dr.		Mach. & Tools Dr.		Vouchers Pay. Acct. Cr.		Sundry Accts. Dr.			When & How Paid			
						Amt.		Name of acct.	Date	Ck. No.	Amt.	

780. Vouchers are prepared in a great variety of forms. In some forms, the check issued in payment of the voucher is included as part of it, while in other forms the check is omitted which, under ordinary conditions, is preferable, as voucher accounts may be paid by note or in other ways, as well as by check.

781. Illustration 125 shows the open voucher or "folder" as it is sometimes called. Illustration 126 shows the back of the same voucher folded, with debit accounts indicated.

782. Vouchers are recorded in a vouchers payable book, or vouchers register. The form of this book varies, to conform with the classification of accounts in the general ledger, and usually contains a separate column for each account that is likely to be debited, with an additional column to receive items for which a separate column is not provided. Illustration 124 shows the form of a vouchers payable book, designed to receive the entries of a manufacturing business conducting a cost system of accounts, with separate columns for the various cost and expense accounts called for in the trial balance shown in illustration 108. The footings of these columns are posted in the general ledger to the debit of the accounts named, at the end of each month, while the total footing of the vouchers payable column is posted to the credit of vouchers payable account. The vouchers payable account is debited at the end of each month from the cash book, notes payable book or other books receiving entries for payments of vouchers, in each of which a separate column should be kept to receive such items. The balance of the vouchers payable account in the general ledger shows the balance owing on unpaid vouchers, *i.e.*, bills that have been vouchered and recorded, but not paid.

Voucher No._____

Date_____ 19__

Name_____

Paid by_____

$_____

MATERIALS		
PROD. LABOR		
SELLING EXP: Advertising		
Other Exp.		
ADMINIS. EXP.		
TOOLS & MACH.		
OTHER ACCTS.		
Total		

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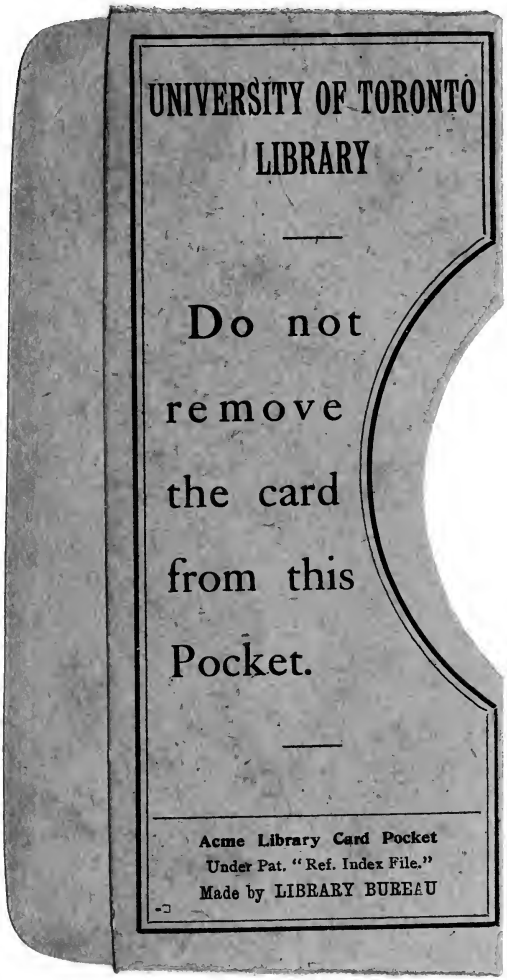
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